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A TREATISE ON THE LAW

PERTAINING TO

CORPORATE FINANCE

INCLUDING

THE FINANCIAL OPERATIONS AND ARRANGEMENTS
OF PUBLIC AND PRIVATE CORPORATIONS

AS DETERMINED BY

THE COURTS AND STATUTES
OF THE UNITED STATES AND ENGLAND

By
WILLIAM A. REID
OF THE NEW YORK BAR

IN TWO VOLUMES
VOL. II

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§ 341. **Rules generally.**— No better evidence need be produced to prove the insolvency of a bank than a return of *nulla bona* made by a sheriff upon executions issued against it.[1] A check does not become absolutely and under all circumstances the property of a bank when deposited in it for collection and the bank gives credit for it upon its books. Should the bank fail while the check is still in its hands and before it has been sent out for collection, it may be recalled by the depositor. If in such case, a receiver be appointed for the bank and the depositor demands the check of him, the receiver ought to charge the account of the depositor with the amount and return the check to the depositor.[2] Among other questions before the federal courts growing out of the insolvency of this national bank and the right to various assets coming into the hands of its receiver,

[1] Wheelock *v.* Kost, (1875) 77 Ill. 296.

[2] Balbach *v.* Frelinghuysen, 6 N. J. Law J. 105.

was this, whether a bank, which had sent it a draft for collection, which it in turn remitted to its correspondent bank at the residence of the owner, and the draft was paid to the latter, the latter not having remitted to the insolvent bank or the latter given the owner of the draft credit for the avails up to the time it was declared insolvent, could recover the proceeds of this collection from the correspondent bank. The United States Circuit Court for the district of Massachusetts held that, until this remittance was made, or the principal bank had given the original owner of the draft credit for the avails, the original owner of the draft, as the owner of the proceeds thereof, was entitled to recover them from the correspondent bank. That though the correspondent was the agent of the bank sending it the draft, and payment to it was to that extent a payment to the principal, yet, until the proceeds were actually remitted to such principal, and mingled with its general funds, or were so credited, the owner of the draft had the option to decline to consider it his debtor, and to claim the proceeds in the hands of the agent, and when the principal failed, and a receiver was appointed, the receiver took the proceeds of the draft when remitted to him, subject to the same right of reclamation by the owner that the latter had as against the agent.[1] A national bank becoming insolvent and being placed in the hands of a receiver, pursuant to the National Banking Association Act, the rights and liabilities of debtors and creditors of the bank become fixed at the appointment of the receiver, and upon his appointment its property is subject, after prior government claims, if any, to disposal and ratable distribution, upon principles of equity, among all its general creditors.[2] Upon the insolvency of a bank, and its affairs going into the hands of a receiver, general depositors must be paid *pro rata*.[3] In the event of a bank becoming insolvent and its affairs being administered through a receivership, one who has made a general deposit of trust funds in it, in good faith on the part of himself and the bank, establishing the relation of debtor and creditor between them, can be given no preference over other general depositors.[4] It appeared in a New Jersey case that on a

[1] National Exchange Bank of Dallas *v.* Beal, (1892) 50 Fed. Rep. 355; affirmed in Beal *v.* National Exchange Bank of Dallas, (1893) 55 Fed. Rep. 894.

[2] Balch *v.* Wilson, 25 Minn. 299.

[3] McLain *v.* Wallace, (1885) 103 Ind. 562.

[4] Fletcher *v.* Sharpe, (1886) 108 Ind. 276.

certain day the directors of a bank discovered that its cashier had embezzled its funds, but not to such an extent, as they then supposed, as to render the bank insolvent, and the bank continued business. The next day a customer of the bank deposited with the bank about $600 in cash and checks, which were credited in his bank book, and the checks duly forwarded for collection, and credited to the bank by its correspondent. The next day the bank suspended through insolvency. The claim of this depositor was held to have no preference in payment over those of other depositors.[1] In its control of a savings bank, in a deficiency of assets to pay its depositors in full, the New Jersey Chancery Court held that a deposit in the bank, under a family agreement, of a sum of money, to pay $1,460 per annum to the widow for life, and the surplus of income from such deposit, if any, to her children, which the bank had received under authority of its charter to accept and execute any trusts committed to it, by any person, by will or otherwise, or by order of any court, was not entitled to preference in payment over others; that, even if the trust claimed for it had been shown, nothing in the charter of the bank gave the fund the priority claimed for it, and it would not be entitled to it.[2] A state court is not deprived by anything in the National Banking Association Law of jurisdiction to determine and segregate a trust fund held by the receiver of an insolvent national bank, and to render judgment for a proper disposal of the fund in accordance with the trust.[3] An indorser of a promissory note, in an action against him by the receiver of an insolvent national bank, cannot defend by a claim of set-off for money deposited in the bank.[4] The United States Circuit Court

[1] Terhune *v.* Bank of Bergen County, 7 Stew. Eq. (N. J.) 367.

[2] Vail *v.* Newark Savings Institution, 5 Stew. Eq. (N. J.) 627. As to the liabilities of a national banking association to which its assets when in the hands of a receiver will be applied and ratably divided among, see Turner *v.* First National Bank, 26 Iowa, 562. For a case holding that where money had been placed with a bank for payment of certain bonds issued by a public corporation, but the owner of the bonds had not presented them for payment when they fell due, and the bank failed, the loss should fall upon the corporation issuing the bonds, and not upon the holder of the bonds, see Adams *v.* Hackensack Improvement Commission, 15 Vroom (N. J.), 638.

[3] Flint Road Cart Co. *v.* Stephens, (1888) 32 Mo. App. 341. As to a state court's jurisdiction to follow the proceeds of certain drafts in the hands of a receiver of a national bank as trust property and to decree their payment to the parties entitled, see Tuttle *v.* Frelinghuysen, 11 Stew. Eq. (N. J.) 12.

[4] Stephens, Receiver, *v.* Schuchmann, (1888) 32 Mo. App. 333.

of Appeals for the third circuit has held that the indorser of a note which is discounted by a national bank, and which matures after the bank becomes insolvent and a receiver was appointed, was entitled to set off against the note the amount of his deposits in the bank at the time of its failure.[1] In an action by the receiver of a national bank upon a note due the bank from two persons jointly, at the time of his appointment, the Minnesota Supreme Court held that promissory notes not due at the time of the appointment of the receiver, upon which the bank and others were liable as makers, and owned at that time by one of the defendants only, and originating in a different transaction, could not be offset against the claim of the receiver on the joint note.[2] In case of an assignment of a bank for the benefit of creditors

[1] Yardley *v.* Clothier, (1892) 51 Fed. Rep. 506, affirming 49 Fed. Rep. 337. The court cited and commented upon Skiles *v.* Houston, 110 Pa. St. 254; s. c., 2 Atl. Rep. 30; Bosler's Admr. *v.* Bank, 4 Pa. St. 32; In re Middle Dist. Bank, 1 Paige, 584; Van Waggoner *v.* Gas Light Co., 23 N. J. Law, 283; Hade *v.* McVay, 31 Ohio St. 231; Clarke *v.* Hawkins, 5 R. I. 224; Balbach *v.* Frelinghuysen, 15 Fed. Rep. 685, and disapproved of Armstrong *v.* Scott, 36 Fed. Rep. 63, and Stephens *v.* Schuchmann, 32 Mo. App. 333.

[2] Balch *v.* Wilson, 25 Minn. 299. In Scnierenberg *v.* Stephens, (1888) 32 Mo. App. 314, and Nichols *v.* Stephens, (1888) 32 Mo. App. 330, it appeared that a national bank had determined in due form to increase its capital stock from $300,000 to $500,000, but the new stock subscriptions never exceeded the sum of $130,000, whereupon the bank advertised an increase to $430,000, but this assumed increase was never authorized by a vote of the stockholders and was never certified to the United States comptroller of the currency, or by him approved or certified. The plaintiffs in these suits had subscribed and paid in certain sums for so much of the proposed addition to the original stock of $200,000. The bank becoming insolvent, it was held that the plaintiffs never became stockholders, and were entitled to be treated as creditors to the amount paid in by them and to have judgment against the receiver for payment of the same in due course of his administration of the assets of the bank. In Flint Road Cart Co. *v.* Stephens, (1888) 32 Mo. App. 341, it appeared that a sum of money had been placed in the hands of the cashier of an insolvent national bank to indemnify him as surety on an attachment bond in behalf of the cart company. The cashier had mingled it with the bank's funds so that it went with the assets of the bank into the hands of the receiver. It was held that the sum of money was a trust fund separate from the general assets of the bank, and upon the discharge of the surety's obligation the company was entitled to recover it from the receiver without any reference to his administration upon the claims of the bank's creditors. For a case showing under what circumstances a contract with other parties by the cashier of a bank which subsequently became insolvent would inure to the benefit of the bank, see Hayes *v.* Orr, (1891) 47 Fed. Rep. 286.

the holders of its notes are entitled to a preference over the holders of certificates of deposit.[1] The noteholders of a bank, after a demand and refusal, will be entitled to interest on their claims in preference to depositors.[2] Where a state bank, organized as a national bank, becomes insolvent, a judgment debt due to it as a national bank cannot be paid in the notes of the old state bank.[3] Where a bank orders its correspondent bank to place to its credit with another bank the balance due it, and by mistake the correspondent places an amount in excess of what is due to the credit of that bank, upon an assignment by the latter, and its assignee receiving the amount from the bank with which it had been credited, the bank making the mistake may recover this excess from the assignee of the assigning bank.[4] Upon stopping payment by a national bank, a debtor to the bank cannot set off a claim subsequently assigned to him.[5] It has been held in the federal court for the eastern district of Virginia that where insolvent debtors of an insolvent national bank assign, giving preferences in favor of the bank, where there is nothing in the language of the assignment, or in the circumstances under which the debt was created, to negative the presumption that the debt should bear interest, and nothing in the conduct of the receiver of the national bank to estop him from claiming interest, interest must be paid.[6]

§ 342. **Appointment of a receiver for national bank.**— The power vested in the comptroller of the currency by the National Banking Act, authorizing him, whenever he becomes satisfied of the insolvency of a national bank, to appoint a receiver, has been held to be discretionary, and his decision as to the insolvency of a bank, for the purpose of such an appointment, held to be final and not reviewable by the court. And the comptroller's right to appoint a receiver under that act is not affected by the right given to stockholders of national banks by United States Revised Statutes, section 5220, to put a bank in voluntary liquidation. Neither is the power of the comptroller to take action,

[1] Pennsylvania Bank Assignees' Account, 39 Pa. St. 103.

[2] Bank of Pennsylvania's Estate, 60 Pa. St. 471.

[3] Thorp *v.* Wegefarth, 56 Pa. St. 82.

[4] First Nat. Bank of Omaha *v.* Mastin Bank, (1880) 48 Fed. Rep. 433.

[5] Venango Bank *v.* Taylor, 56 Pa. St. 14.

[6] Bain *v.* Peters, (1890) 44 Fed. Rep.

before the bank ceases to do a banking business, limited by the provision of the statute, that after the receiver has had charge of the bank long enough to pay all its debts the stockholders may select an agent to take charge of such assets as remain. And the provision of the act, authorizing the appointment of a receiver by the comptroller to "close up" a national banking association, contemplates the liquidation and final winding up of the business of the bank, not the mere closing of the bank, and does not limit the power of the comptroller to take action before the bank has closed its doors.[1]

§ 343. **When an appointment of receiver of a bank is not authorized.**— A demurrer to an action brought by one appointed by a court receiver of a bank in California was sustained in the United States Circuit Court for that district. The court held that the statute of that state authorizing the attorney-general, on the recommendation of the bank commissioners, to institute suit to enjoin any bank guilty of violating the banking laws from doing further business, and if the bank be found insolvent to cause its business to be wound up under the direction of the bank commissioners, did not authorize the court to appoint a receiver for the bank; and a receiver appointed in such a proceeding and manner was without authority to maintain a suit to collect claims of the bank. It was further held that the statute of the state providing that upon the "dissolution of any corporation" a receiver may be appointed on the application of creditors or stockholders, did not apply to the case of an insolvent bank which the state was proceeding against for violating its charter.[2]

§ 344. **Powers of a receiver for a national bank.**—Section 5234 of the United States Revised Statutes, referring to receivers appointed for national banking associations becoming insolvent, provides as follows: "Such receiver, under the direction of the comptroller, shall take possession of the books, records and assets of every description of such association, collect

[1] Washington Nat. Bank of Tacoma v. Eckels, (1893) 57 Fed. Rep. 870.

[2] Murray v. American Surety Co. of New York, (1894) 59 Fed. Rep. 345; reaffirmed in Murray v. American Surety Co. of New York, (1894) 61 Fed. Rep. 273.

all debts due and claims belonging to it, and, upon the order of a court of record of competent jurisdiction, may sell or compound all bad or doubtful debts, and, on a like order, may sell all the real and personal property of such association on such terms as the court shall direct, and may, if necessary to pay the debts of such association, enforce the individual liability of the stockholders." An application was made in the United States District Court for the southern district of California for an order authorizing the receiver of an insolvent national banking association within that jurisdiction to compound the statutory liability of certain of its stockholders. Ross, D. J., denied the petition.[1]

§ 345. **Actions of such receivers — rules.**— A receiver of a national bank may sue in the United States Circuit Court to recover an indebtedness owing to the bank, without regard to the amount involved.[2] A national bank which had pledged nego-

[1] In re Certain Stockholders of the California Nat. Bank of San Diego, (1892) 53 Fed. Rep. 38. These were the reasons given for the court's action: "Assuming that the court is authorized to grant the order asked for, it is unhesitatingly refused. To sanction proceedings by which a stockholder in a national banking association fraudulently puts away his property for the purpose of avoiding his just and legal obligations as such stockholder, and is then permitted to compromise his liability for the payment of a less sum than is due, is to place a premium upon fraud. With such conduct there should be no compromise. Laws are made to be observed and enforced, and every one should be made to know that, in respect to every contract made pursuant to these provisions, the government will accord and exact fair dealing and the utmost good faith. It is far better that the entire amount of the obligations of the stockholders in question should be lost to the trust fund than that the slightest judicial countenance should be given the proposed proceedings. The liability of the stockholders of the insolvent bank is several, not joint. Kennedy *v.* Gibson, 8 Wall. 505. And there is no reason why the property of every one who has conveyed or may convey it for the fraudulent purpose of avoiding his first and legal obligations arising under the law should not be followed and every reason why it should be. * * * It is, however, to say the least, extremely doubtful whether the court has the power to authorize the compromising of the statutory liability of a stockholder in a national bank. * * * It is by no means clear that the statutory liability of the stockholders is a debt within the meaning of the clause authorizing the court to sanction the compounding of all bad or doubtful debts." This point, however, was not decided, it not being necessary.

[2] Yardley *v.* Dickson, (1891) 47 Fed. Rep. 835. See U. S. *v.* Mooney, 116 U. S. 104; s. c., 6 Sup. Ct. Rep. 304; Kennedy *v.* Gibson, 8 Wall. 498; Frelinghuysen *v.* Baldwin, 12 Fed. Rep. 395; Platt *v.* Beach, 2 Ben. 303; Stanton *v.* Wilkeson, 8 Ben. 357; Price *v.* Abbott, 17 Fed. Rep. 506; U. S. *v.* Shaw, 39

tiable notes to another bank to secure a loan became insolvent. The bank to which the notes had been pledged held them after a receiver for the insolvent bank had been appointed, still taking steps to collect them on account of a balance of its loan. Those who had obtained judgments against the insolvent bank in the state courts had by garnishment proceedings sought to enforce their claims against the proceeds of these notes in the hands of the bank holding them. The Circuit Court of the United States, in which the receiver brought his action in equity against this bank, and the creditors endeavoring to enforce their claims against the insolvent bank in the state courts, to recover the control of these notes as a part of the assets of the insolvent bank, that he might distribute the proceeds as other assets, upon a demurrer filed by the respondents, sustained the jurisdiction of the Court of Equity in the matter.[1] The receiver of an insolvent national bank, it has been held, may at any time dismiss an attorney employed by him, regularly or otherwise, to prosecute claims of the bank, and employ another in his place, when the court will, by order, substitute him in the place of the dismissed attorney, except as to such cases as the latter may have commenced and finished. But where a contract has been entered into between the receiver and the attorney that the latter should receive the attorney's fees provided for in the notes he was employed to collect, the court will not direct the substitution of another attorney in unfinished cases until the receiver deposits the amount of the attorney's fees reserved in the notes as a security to the dismissed attorney for such services as he may have rendered.[2] The maker of a note upon which the receiver of a national bank has brought action may plead as set-off any debt of the bank to him existing at the time of its failure, as the receiver takes the choses in action belonging to the bank subject to all claims and defenses which might have been interposed as against the bank before the liens of the United States and general creditors attached.[3] Where a bank has received the proceeds of a fraudulent sale of stock belonging to it, the fact that a receiver for the bank is subse-

Fed. Rep. 433; Mitchell *v.* Walker, 2 Browne Nat. Bank Cas. 180; Hendee *v.* Railroad Co., 26 Fed. Rep. 677.

[1] Chase *v.* Cannon, (1891) 47 Fed. Rep. 674, the court considering the case in its important features similar to Bank *v.* Mixter, 124 U. S. 721; s. c., 8 Sup. Ct. Rep. 718.

[2] In re Herman, (1892) 50 Fed. Rep. 517.

[3] Adams *v.* Spokane Drug Co., (1893) 57 Fed. Rep. 888, following Yardley *v.*,

quently appointed does not give its creditors such right in the proceeds as will prevent the purchaser of the stock rescinding the order and requiring restitution.[1] A state bank of Ohio discounted its note payable to the order of its cashier and indorsed by him with a national bank in Ohio for a sum of money which was to remain on deposit to the credit of the former bank in the latter, subject to its check. It had drawn but a small amount of this deposit when the national bank was taken in charge by the comptroller of the currency, on account of its insolvency, and placed in the hands of a receiver for the purpose of winding up its affairs. The receiver brought action against the state bank and its cashier upon its note. The bank claimed the right to set off the balance on deposit, tendering the amount which it had drawn by its checks. Judgment upon a demurrer to the answers was given in favor of the receiver. The bank then filed its bill in equity for injunction to restrain the collection of the judgment, and claiming the same right to set-off. This bill was dismissed on demurrer in the United States District Court, and among others, upon appeal to the United States Circuit Court of Appeals the latter court certified to the United States Supreme Court, for its opinion, the following question: "Where a national bank becomes insolvent, and its assets pass into the hands of a receiver appointed by the comptroller of the currency, can a debtor of the bank set off against this indebtedness the amount of a claim he holds against the bank, supposing the debt due from the bank to have been payable at the time of its suspension, but that due to it to have been payable at a time subsequent thereto?" The Supreme Court of the United States answered this question affirmatively.[2]

Clothier, 49 Fed. Rep. 337; Pauly *v.* State Loan & Trust Co., 56 Fed. Rep. 430; affirmed by United States Circuit Court of Appeals in Pauly *v.* State Loan & Trust Co., 58 Fed. Rep. 666.

[1] Merrill *v.* Florida Land Imp. Co., (1893) 60 Fed. Rep. 17, affirming 52 Fed. Rep. 77; s. c, 2 C. C. A. 629; 2 U. S. App. 434.

[2] Farmers & Merchants' State Bank *v.* Armstrong, (1892) 146 U. S. 499. The charter of the national bank was forfeited and the bank dissolved by a decree of the Circuit Court, July 12, 1887, when title to its assets was necessarily thereby transferred to the receiver. National Bank *v.* Colby, 21 Wall. 609. After stating this fact, FULLER, Ch. J., speaking for the court, *arguendo*, said: "The note in controversy did not mature until September 7, 1887, but the deposit to the credit of the Farmers' Bank was due for the purposes of suit upon the closing of the Fidelity Bank [the one in hands of receiver], as under such circumstances no demand was necessary. The receiver took the assets of

§ 346. Actions to control the conduct of such receivers.—The United States Circuit Court for the western district of Washington sustained the removal of a suit from the state court, the object of which suit was to control the action of the receiver of a national bank appointed by the comptroller of the currency. It was held that in such an action, to secure the application of

the Fidelity Bank as a mere trustee for creditors, and not for value and without notice, and, in the absence of statutes to the contrary, subject to all claims and defenses that might have been interposed as against the insolvent corporation before the liens of the United States and of the general creditors attached. The right to assert set-off at law is of statutory creation, but courts of equity, from a very early day, were accustomed to grant relief in that regard independently as well as in aid of statutes upon the subject. In equity, relief was usually accorded, says Mr. Justice STORY (Eq. Jur. § 2435), 'where, although there are natural and independent debts, yet there is a natural credit between the parties, founded, at the time, upon the existence of some debts due by the crediting party to the other. By natural credit, in the sense in which the terms are here used, we are to understand, a knowledge on both sides of an existing debt due to one party, and a credit by the other party, founded on and trusting to such debt, as a means of discharging it.' This definition is hardly broad enough to cover all the cases where, as the learned commentator concedes, there being a 'connection between the demands, equity acts upon it, and allows a set-off under particular circumstances.' § 1434. Courts of equity frequently deviate from the strict rules of mutuality when the justice of the particular case requires it, and the ordinary rule is that where the mutual obligations have grown out of the same transaction, insolvency on the one hand justifies the set off of the debt due upon the other. Blount *v.* Windley, 95 U. S. 173, 177. In Carr *v.* Hamilton, 129 U. S. 252, 262, it was decided that, when a life insurance company becomes insolvent and goes into liquidation, the amount due on an endowment policy, payable in any event at a fixed time, may, in settling the company's affairs, be set off against the amount due on a mortgage deed from the holder of the policy to the company by way of compensation; and Mr. Justice BRADLEY, delivering the opinion of the court said: 'We are inclined to the view that where the holder of a life insurance policy borrows money of the insurer, it will be presumed, *prima facie*, that he does so on the faith of the insurance and on the expectation of possibly meeting his own obligation to the company by that of the company to him, and that the case is one of mutual credits, and entitled to the privilege of compensation or set-off whenever the mutual liquidation of the demands is judicially decreed on the insolvency of the company.' And the case of Scammon *v.* Kimball, 92 U. S. 362, was referred to, where it was held that a bank, having insurance in a company which was rendered insolvent by the Chicago fire of 1871, had a right to set off the amount of his [its?] insurance on property consumed against money of the company in his [its?] hands on deposit, although the insurance was not a debt due at the time of the insolvency. Indeed, natural justice would seem to require that where the transaction is such as to raise the pre-

part of the funds in the hands of a receiver appointed by the comptroller of the currency in satisfaction of plaintiff's claim against the insolvent bank for money received by it as collecting agent, the bank was only a nominal party, the receiver being the one to be held accountable for any unauthorized disposition of the money sued for; and, since the object of this suit was to control

sumption of an agreement for a set-off, it should be held that the equity that this should be done is superior to any subsequent equity not arising out of a purchase for value without notice. In the case at bar the credits between the banks were reciprocal and were parts of the same transaction, in which each gave credit to the other on the faith of the simultaneous credit, and the principle applicable to mutual credits applied. It was, therefore, the balance upon an adjustment of the accounts which was the debt, and the Farmers' Bank had the right as against the receiver of the Fidelity Bank, although the note matured after the suspension of the bank, to set off the balance due upon its deposit account, unless the provisions of the National Banking Law were to the contrary. * * * The argument is that [sections 5234, 5236 and 5242, Rev. Stats. U. S.] by implication forbid this set-off because they require that after the redemption of the circulating notes has been fully provided for, the assets shall be ratably distributed among the creditors, and that no preferences given or suffered, in contemplation of or after committing the act of insolvency, shall stand. And it is insisted that the assets of the bank, existing at the time of the act of insolvency, include all its property without regard to any existing liens thereon or set-off thereto. We do not regard this position as tenable. Undoubtedly, any disposition by a national bank, being insolvent or in contemplation of insolvency, of its choses in action, securities or other assets made to prevent their application to the payment of its circulating notes, or to prefer one creditor to another, is forbidden; but liens, equities or rights arising by express agreement, or implied from the nature of the dealings between the parties, or by operation of law, prior to insolvency and not in contemplation thereof, are not invalidated. The provisions of the act are not directed against all liens, securities, pledges or equities, whereby one creditor may obtain a greater payment than another, but against those given or arising after or in contemplation of insolvency. Where a set-off is otherwise valid, it is not perceived how its allowance can be considered a preference, and it is clear that it is only the balance, if any, after the set-off is deducted which can justly be held to form a part of the assets of the insolvent. The requirement as to ratable dividends is to make them from what belongs to the bank, and that which at the time of the insolvency belongs of right to the debtor does not belong to the bank. There is nothing new in this view of ratable distribution, As pointed out by counsel, the bankruptcy act of 13 Eliz., chap. 7, contained no provision in any way directing a set-off or the striking of a balance, and by its second section, commissioners in bankruptcy were to seize and appraise the lands, goods, money and chattels of the bankrupt, to sell the lands and chattels, or otherwise to order the same for the satisfaction and payment of the said creditors a portion, rate and rate alike, according to the quantity of his or

the official conduct of the receiver, appointed under the authority of the national banking laws, and his defense must rest on the interpretation of those laws, the case was within the jurisdiction of the federal Circuit Court as being one "arising under the * * * laws of the United States."[1]

§ 347. **What a receiver cannot set off in an action to recover trust funds coming into his hands.**— The United States Circuit Court of Appeals for the third circuit affirmed the holding of the court below in this case, that the debts of a partner and his firm to a bank could not, in equity, be set off by a receiver of a bank against trust moneys which the partner, after

their debts. 4 Statutes of the Realm, part 1, 539. Yet in the earliest reported decisions upon set-off it was allowed under this statute. Anonymous, 1 Mod. 215; Curson *v.* African Co., 1 Vern. 121; Chapman *v.* Derby, 2 Vern. 117. The succeeding statutes were but in recognition, in bankruptcy and otherwise, of the practice in chancery in the settlement of estates, and it may be said that in the distribution of the assets of insolvents under voluntary or statutory trusts for creditors, the set off of debts due has been universally conceded. The equity of equality among creditors is either found inapplicable to such set-offs or yields to their superior equity. We are dealing in this case with an equitable set-off, but if on June 20 [the day the bank was ordered closed] the note had matured and each party had a cause of action capable of enforcement by suit at once, upon the argument for the receiver, the legal set off would be destroyed just as effectually as it is contended the equitable set-off is. We cannot believe congress intended such a result, or to destroy by implication any right vested at the time of the suspension of a national bank. The state of case where the claim sought to be offset is acquired after the act of insolvency is far otherwise, for the rights of the parties become fixed as of that time, and to sustain such a transfer would defeat the object of these provisions. The transaction must necessarily be held to have been entered into with the intention to produce its natural result, the preventing of the application of the insolvent's assets in the manner prescribed. Venango National Bank *v.* Taylor, 56 Pa. St. 14; Colt *v.* Brown, 12 Gray, 233. Our conclusion is that this set-off should have been allowed, and this has heretofore been so held in well-considered cases. Snyder's Sons Co. *v.* Armstrong, 37 Fed. Rep. 18; Yardley *v.* Clothier, 49 Fed. Rep. 337; Armstrong *v.* Warner, 21 Weekly L. Bull. 136; 27 Weekly L. Bull. 100."

[1] Grant *v.* Spokane Nat. Bank, (1891) 47 Fed. Rep. 673; citing Armstrong *v.* Ettlesohn, 36 Fed. Rep. 209; Armstrong *v.* Trautman, 36 Fed. Rep. 275; McConville *v.* Gilmour, 36 Fed. Rep. 277; Sowles *v.* Witters, 43 Fed. Rep. 700; Tennessee *v.* Davis, 100 U. S. 257–264; Railroad Co. *v.* Mississippi, 102 U. S. 135–141; Removal Cases, 115 U. S. 11; s. c., 5 Sup. Ct. Rep. 1113; Bachrack *v.* Norton, 132 U. S. 337; s. c., 10 Sup. Ct. Rep. 106; Feibelman *v.* Packard, 109 U. S. 421–423; s. c., 3 Sup. Ct. Rep. 289; Reagan *v.* Aiken, 138 U. S. 109; s. c., 11 Sup. Ct. Rep. 283; Bock *v.* Perkins, 139 U. S. 630; s. c., 11 Sup. Ct. Rep. 677.

the debts were contracted, mingled with the firm's deposits without the bank's knowledge, and the whole amount of which remained continuously in the bank until it failed.[1]

§ 348. When a receiver cannot question the disposition of funds coming into the hands of a clearing house association.— It appeared in this case that, by special agreement, a national bank of Philadelphia, instead of the usual deposit of securities as collateral for payment of its daily balance at the clearing house of that city, each day left with the manager of the clearing house all checks drawn on it, and other evidences of its indebtedness received from other banks, to be held until the balance due from it for the day was paid. While certain checks and other evidences of its indebtedness were so held, the bank was closed by the comptroller of the currency. Upon this happening the clearing house collected the amount of the checks and other evidences of indebtedness from the banks from which they

[1] Fisher *v.* Knight, (1894) 61 Fed. Rep. 491, affirming Knight *v.* Fisher, (1893) 58 Fed. Rep. 991. ACHESON, Circuit Judge, *arguendo*, said: "There is abundant authority for the doctrine that the real ownership of a fund deposited in a bank may be shown to be in another than the person in whose name the deposit is made; and the fund recovered from the bank by the true owner, if the bank has not been misled or prejudiced by the apparent ownership. Frazier *v.* Bank, 8 Watts & S. 18; Stair *v.* Bank, 55 Pa. St. 364; Bank *v.* King, 57 Pa. St. 202. Upon the admitted facts, and under the authorities, we are of the opinion that the fund in controversy belonged to the plaintiff and was recoverable by him from the bank or its receiver. The court below was clearly right in holding that the defendant could not set off against the plaintiff's claim the liability of N. T. Lewis as a stockholder of the bank, or the amount of the note for one thousand dollars. The liability of Lewis upon his assessment was altogether his individual debt, and in no view of the case was it a proper set-off. Noreross *v.* Benton, 38 Pa. St. 217. Neither the bank nor the receiver had done anything upon the faith of the apparent ownership of the fund, and neither was prejudiced in consequence of the deposit having been made in the name of N. T. Lewis & Son. The note was not taken on the credit of the deposit. It was discounted thirty days before the plaintiff's money came into the bank. Nearly two months had elapsed after the closing of the bank before the note matured. The bank had no lien upon the deposit for a debt not due. Jordan *v.* Bank, 74 N. Y. 467, 472. The rights of the parties were fixed upon the insolvency of the bank and the appointment of the receiver. As the defendant had no right then to apply the plaintiff's money to pay the debt of N. T. Lewis & Son, he has no such right now. Certainly, the mere delay of the plaintiff in bringing suit until after the maturity of the note did not change the situation."

had been received, and from the amount realized paid, besides the bank's balance for the day, due bills given by it for its balances for the preceding day, by their terms payable only through the clearing house the day after issue, and actually in the exchanges held when the bank closed, and applied the remainder towards cancellation of clearing house loan certificates issued to the bank under an agreement between the banks whereby any loss from failure of one to pay such certificates was chargeable upon the others. The receiver of the insolvent bank instituted a suit against the clearing house committee of the Clearing House Association to recover those checks or the money collected thereon, and had a decree in his favor in the Circuit Court. Upon appeal to the United States Circuit Court of Appeals for the third circuit, the appellate court held that, as the transaction on the part of the bank was not in contemplation of insolvency, nor with a purpose to give a preference, or to prevent application of its assets as prescribed by law, the exchange between the banks was valid, and that it was not avoided, nor were the rights of the clearing house or of the creditor banks impaired by what subsequently occurred. Therefore, the receiver of the bank, taking its assets subject to all equities and rights against it, had no equity, in his suit, to question the appropriation of the money paid by the other banks.[1]

§ 349. **Attachment of property of an insolvent bank — retains its lien against a receiver of the bank subsequently appointed.**— A receiver of a bank in Nebraska made a motion to dissolve an attachment which had been levied upon real estate belonging to the bank in the suit of a depositor for the amount of his deposit. The motion was tried upon a stipulation of facts which showed that the attachment was levied properly upon the thirteenth of November; that the bank was then unable to pay its obligations; that before noon of that day the bank suspended business, and posted on its doors a notice as follows: "Bank closed; in hands of receiver; depositors will be paid in full;" that on the morning of that date the managers of the bank telegraphed to the "state banking board" that the bank was closed, and asked the board to send a receiver; that on the four-

[1] Philler *v.* Yardley, (GREEN, D. J., dissenting) (1894) 62 Fed Rep. 645, reversing Yardley *v.* Philler, 58 Fed. Rep. 746.

teenth of November the bank was duly examined by an examiner appointed by the "state banking board," and that on the nineteenth of November the receiver of the bank was appointed by the court. The contention of the receiver was that after the bank suspended business and closed its doors on the thirteenth its property was not subject to attachment at the suit of a creditor, but that all the bank's assets from that moment became a trust fund, to be divided *pro rata* among all the bank's creditors; or, if the property of the bank was subject to attachment on the thirteenth, then the appointment of a receiver on the nineteenth vacated the attachment. The Supreme Court of that state held that the lien acquired by the creditor of the bank on the real estate of the bank by the levy of his attachment thereon was not dissolved by the appointment of a receiver to take charge of the assets of the bank, and, as the creditor's lien was acquired prior to the appointment of the receiver, that officer took the property attached incumbered with the lien.[1]

[1] Arnold *v.* Weimer, (Neb. 1894) 58 N. W. Rep. 709. In disposing of the contention of the receiver the court first showed that there was no express statute or provision in the State Banking Act which sustained his contention, and then proceeded to discuss the questions involved in these words: "Another argument of the receiver is that, inasmuch as the assets of a national bank are not liable to be attached at the suit of a creditor, the legislature must have intended, by the enactment of the Banking Law of this state, that the assets of an insolvent banking association, from the moment of its insolvency, should occupy the same status as the assets of an insolvent national bank. If the legislature had intended by the Banking Act to render the property of an insolvent bank exempt from an attachment of the suit of one of its creditors, it would doubtless have said so. The National Banking Act expressly provides that the United States shall have a first and paramount lien upon all the assets of the bank, and that no attachment shall be issued against said association or its property till the final judgment rendered in the suit brought. Counsel for the receiver cites us to State *v.* Commercial State Bank, 28 Neb. 677; s. c., 44 N. W. Rep. 998, as an authority for the contention. In that case one McConaughy was a large stockholder in the Commercial State Bank. He (McConaughy) became insolvent, and made an assignment to the sheriff for the benefit of his (McConaughy's) creditors. The sheriff took possession of not only McConaughy's property, but claimed the right to the possession of the assets of the bank as well. The attorney-general made application to this court for the appointment of a receiver for the assets of the bank. The sheriff, as McConaughy's assignee, resisted the application, claiming that McConaughy owned all the stock in the bank. The court, by the present Chief Justice NORVAL, held, in effect, that, although McConaughy was the owner of the majority of all the stock of the corporation, he did not thereby

§ 350. Claims against an insolvent bank — jurisdiction of court appointing receiver.—A bank in the state of Michigan presenting a claim for a note which had been rediscounted with it and indorsed by a savings bank of that state to a receiver in whose hands the latter was under the banking laws of that state for winding up its affairs, and being refused payment by the receiver, petitioned the Circuit Court praying that an issue might be framed for the trial of the liability of the insolvent bank to the former on the note to be entered upon the law side of the court. This petition was refused on the ground that under the General Banking Law of the state the court had no jurisdiction in the matter,

become the corporation; and that while his assignee could hold his (McConaughy's) property, the assignee had no claim to the assets of the bank; that they were a trust fund for the payment of its debts, and that the rights of creditors to the bank's property were superior to the rights of the stockholders and the assignee of the stockholders thereto. Nothing in that case supports the contention made by the receiver. There being no statutory provision which exempts the property of this bank from attachment at the suit of one of its creditors prior to the appointment of a receiver therefor, or possession taken by the sheriff under [the statute of this state], and no provision creating an attachment already levied upon the appointment of a receiver for its assets, we proceed to inquire what right or title the receiver acquired to the property attached by virtue of his appointment. [Our statute] provides that the order of attachment shall bind the property attached from the time of the service of the order. * * * In Beach on Receivers (§ 202) it is said: 'It is a general rule that the receiver obtains title subject to all liens previously acquired, but this rule is applicable only to property which is subject to levy and sale under execution. As to other property — such, for example, as equitable interests — the commencement of the action for the appointment of a receiver creates a lien in favor of the plaintiff.' The real estate attached [in this suit] was subject to levy and sale under execution. The legal title to this property was in the bank. A question very similar to the one at bar arose and was decided in Hubbard *v.* President, etc., 7 Met. (Mass.) 340. In that case the Phœnix Bank stopped payment on the 3d day of October, 1842, and afterwards, on the same day, the Hamilton Bank brought suit against the Phœnix Bank in the Common Pleas Court in Suffolk county, and had an attachment issued and levied upon the real and personal property of the Phœnix Bank. On the sixth of October, 'on the application of the bank commissioners,' the Supreme Court of Massachusetts issued an injunction restraining the Phœnix Bank from transacting any further business until a hearing could be had. On the eighteenth of October the Supreme Court appointed a receiver to take possession of the assets of the Phœnix Bank. The receiver then filed a petition in the Supreme Court praying it to enjoin the Hamilton County Bank from further prosecuting its suit at law against the Phœnix Bank, and to dissolve the attachment levied upon the property of the Phœnix Bank. The court, by DEWEY, J., said: 'This leads us directly to the consideration

but that the remedy of the bank was by suit in the usual form against the insolvent bank. The bank applied to the Supreme Court of the state for a *mandamus* to compel the Circuit Court to order such issue to be framed and proceed to the trial of the cause. There was a contention on the hearing that, inasmuch as the state itself did not expressly confer power upon the court appointing the receiver to take cognizance of the claims presented for allowance against the insolvent savings bank, therefore, no such power could be exercised by the Circuit Court. To this the court said: "Section 55 of the act, in express terms, places the receiver under the direction of the court in taking possession of the property

of the effect to be given an injunction upon a banking corporation and the appointment of a receiver under the statute; and, in connection therewith, and as the material inquiry in the present case, to consider the nature and effect of an attachment or mesne process, and to what extent such attachment constitutes a lien or incumbrance upon the assets of the bank. The power and authority of receivers appointed under the provisions of the statutes referred to are not distinctly defined by this statute, but it is provided in general terms that one of the justices of the court may appoint receivers to take possession of the property and effects of the corporation, subject to such rules and orders as may, from time to time, be prescribed by the Supreme Judicial Court. * * * There is no express provision in the statutes cited dissolving existing attachments upon the transfer of the property of the corporation to receivers similar to that found in the General Insolvent Law; and if such effect follows, it results from general principles governing cases of this nature, rather than by force of any special enactment. * * * We are satisfied that under the laws of Massachusetts an attachment is a lien or incumbrance upon the property attached. It fastens itself upon the property, and whoever takes the property takes it *cum onere*. It is constantly spoken of as a lien in the books of reports, in the arguments of the bar, and in the opinions of the bench. It is not a lien in that sense which requires the party to be in possession of the property thus incumbered or charged with it. An attachment of real estate does not require a change of possession, but that does not make it the less a lien in the sense which we attach to that term. * * * But it is further urged that if such be the rule of law as to the nature and effect of an attachment, yet it is a lien capable of being dissolved, and that by the force and effect of the injunction issued by this court against the Phœnix Bank, and the appointment of receivers to take control and management of the assets of the bank for the benefit of all concerned, the attachment was *ipso facto* dissolved. * * * We think there is a manifest distinction between the case of an attachment before and one made after proceedings instituted praying for an injunction and the appointment of receivers. In the latter case the attachment is ineffectual. The property is in other hands, and beyond the process of an attachment. But in the former case a valid attachment has been made, and, hence, it will bind the property; and although the assets pass into the hands of receivers, they take them with all the liens thereon, and an ex-

and assets of the bank, the collection of claims, compounding of debts, sales of property and the enforcement of the individual liability of stockholders. It is true that the statute fixes the depository of the fund, not with the register of the county, but with the state treasurer, and the distribution is under the direction of the commissioner, but the receiver is nevertheless an officer of the court as much as a receiver appointed in the ordinary way under a bill in chancery. The commissioner of banking does not appoint the receiver. It is done by the court upon the petition of the commissioner approved by the attorney-general; and when the funds are paid into the hands of the receiver, and deposited with the state treasurer, the receiver and not the commissioner makes the ratable dividends. The receiver represents the insolvent bank. Under the statute all claims against it are to be presented to him for allowance, and if he does not allow them the claimant may invoke the aid of the court."[1]

isting attachment is a lien. * * * It seems, therefore, quite clear that there is nothing in the nature of the process by injunction against the Phœnix Bank, and the appointment of receivers which necessarily dissolves an attachment of the assets of the bank previously made. There is nothing in the principle of equal distribution among all creditors *pro rata* which has been considered powerful enough to set aside the priority already acquired by a vigilant creditor. There is nothing in our statutes declaring such previous attachments to be dissolved by force and effect of appointment of receivers.'" The Nebraska court then cited as to the same effect as the Massachusetts case, just referred to, the case of Von Roun *v.* Superior Court, 58 Cal. 358, and Walling *v.* Miller, 108 N. Y. 173; s. c., 15 N. E. Rep. 65. They then said of a Colorado case: "In Breene *v.* Bank, (Col.) 17 Pac. Rep. 280, the Merchants and Mechanics' Bank suspended payment on the afternoon of the 30th of January, 1884. It was then, and had been for some time, insolvent. At the time it closed its doors it was indebted to Breene in the sum of seven thousand dollars, and on that day he brought a suit against the bank to recover the amount due him, and caused an attachment to be issued and levied upon the assets of the bank. Six days later, on application of the stockholders, one Talbot was appointed receiver for the bank. He intervened in the suit brought against the bank by Breene, and filed a notice to dissolve the attachment. The Supreme Court of Colorado held that the creditors of insolvent corporations, as those of other insolvents, have no equitable liens superior to an attachment unless a court of equity lawfully assumes jurisdiction before attachment, and reversed the judgment of the District Court, which had dissolved the attachment on the motion of the receiver."

[1] Citizens' Savings Bank *v.* Person, Circuit Judge, etc., (1893) 98 Mich. 173, 175, 176. The court then said: "It is apparent that the court appointing the receiver has jurisdiction over him and the fund, and may permit any claimant to present his claim in that proceeding, and make his proofs and establish it therein. There can be

§ 351. For what amount claims should be made and allowed.— An allowance by the comptroller of the currency out of the assets of an insolvent national bank to a creditor who brought suit on his claim and reduced it to judgment, for the amount due on the claim at the date of the failure, and the disallowance by him of the claim as it appeared on the face of the judgment, was approved by the Supreme Court of the United States in a suit for *mandamus* to compel the comptroller to pay a dividend on the amount claimed on the face of the judgment.[1]

found in this statute no prohibition upon the court, they having jurisdiction, from proceeding under its general powers to hear and determine the questions arising upon such claims. The claims, under the statute, are not to be presented to the insolvent bank, but to the receiver; and in any action brought to prove such claim against the insolvent bank, the receiver, and not the bank, is necessarily the party interested in contesting it and to insist upon its being properly established by competent evidence. In doing this he is acting as an officer of the court and under its direction. The court, by the appointment of the receiver, has taken into its own hands the subject-matter of the litigation over such claims as may be presented, and holds it pending the proceedings and until the final disposition of all questions, legal and equitable, involved in the action. It would lead to most unseemly struggles if parties having claims against insolvent banks could apply to any other tribunal for such allowance, and thus compel the receiver, who must in all such cases be made the party defendant, to appear in other jurisdictions to defend against the other. To permit the receiver to be sued in any other court upon such claims would not be compatible with the dignity and authority of the court appointing him, and would lead to great inconvenience and cost to the estate which the receiver represents. The proper and orderly manner for the allowance of such claims is by petition to the court appointing the receiver, and in the same action. The practice is for persons having claims against property in the hands of a receiver to intervene in the suit by petition, and have their rights adjudicated. Beach Rec. § 654. The court should grant leave to the petitioner so to intervene and prove his claim, unless it clearly appears that the demand has no legal foundation. The insolvent bank is not the party to be impleaded. The receiver is the only proper party. He has the assets of the bank under his control and is bound to protect the fund for those who are legally entitled to distributive shares. No suit can be brought by or against the receiver without leave of the court appointing him; but that court should in all cases permit the party having the claim to intervene in the proceeding and make proof of it, when he shows a probable cause of action, and in appropriate cases the trial should be upon the law side."

[1] White *v.* Knox, (1884) 111 U. S. 784, affirming the refusal of the *mandamus*. WAITE, Ch. J., for the court, said as to the law in such case: "Dividends are to be paid to all creditors ratably, that is to say, proportionally. To be proportionate they must be made by some uniform rule. They are to be paid on all claims against the bank previously proved

It was claimed by a bank here that had made a loan to this insolvent bank and received from it collaterals to secure that loan, that it was entitled to prove its claim for a dividend from the receiver for the full amount of the original loan notwithstanding it had received money upon a portion of the collaterals.

and adjudicated. All creditors are to be treated alike. The claim against the bank, therefore, must neccessarily be made the basis of the apportionment. If the comptroller is satisfied with the proof which is furnished to him, he can allow the claim, and when the allowance is made the creditor becomes entitled at once to participate in all dividends that may be declared. If the comptroller declines to recognize the claim as valid, it must be established by the adjudication of some competent court before it can share in the distribution of assets. When adjudicated in favor of the creditor it is established as a claim against the bank, and must be treated accordingly by the comptroller. The business of the bank must stop when insolvency is declared. Rev. Stat. § 5258. No new debt can be made after that. The only claims the comptroller can recognize in the settlement of the affairs of the bank are those which are shown by proofs satisfactory to him, or by the adjudication of a competent court, to have had their origin in something done before the insolvency. It is clearly his duty, therefore, in paying dividends, to take the value of the claim at that time as the basis of distribution. If interest is added on one claim after that date before the percentage of dividends is calculated, it should be upon all, otherwise the distribution would be according to different rules, and not ratably as the law requires." There was an insistment in this case, on the part of the relator, that he was entitled to dividends on his judgment, as that was the amount adjudicated to him, and the advantage he would get in this way was no more than just, because of the trouble and expense he was put to in carrying on his litigation, and the delay he had suffered in getting his money. To this the chief justice said: "The question here is not whether he should be paid interest on the several items of percentage which make up the aggregate of sixty-five per cent from the time of the payment of dividends to other creditors until his claim was adjudicated, but whether the amount of his judgment must be taken as the sum on which his dividend is to be paid. As has already been seen, the dividends are to be paid on the adjudicated claim, not on the amount due upon the claim when adjudicated. The judgment established the claim as a claim against the bank at the time of the insolvency, and the amount due when the judgment was rendered. Thus the claim was adjudicated, and the amount due at the date of the judgment ascertained; but for the comptroller to pay the relator on the amount due him at that time, and the other creditors on the amount due them eight years before, when the insolvency occurred, would certainly not be making ratable dividends from the assets on all claims against the bank. It was clearly right, therefore, to ascertain from the judgment how much was due on this claim at the date of the insolvency, and make the distribution accordingly. The trouble and expense which the relator has been put to for the establishment of his claim are but incidents to the business in which he was engaged. It was the duty of the comptroller, if not satisfied of the correctness of the claim

The United States Circuit Court for the southern district of Ohio held, however, that Revised Statutes United States, sections 5235, 5236, which provide respectively that the comptroller on appointing a receiver for an insolvent national bank, shall advertise for proof of claims, and that he shall make a ratable dividend of the moneys paid over to him by the receiver among those who have presented their claims, cannot be construed to fix the date of the suspension of the bank as a date with reference to which all calculations of the amount due to creditors are to be made as a basis for dividends. Therefore, where after such suspension, but before the filing of a claim with the receiver, such claim was reduced by collecting from collaterals, it should have been credited with such collections when filed, and the balance then found due used as the basis for ascertaining claimant's dividend.[1]

§ 352. **What a claimant may be charged with.**— This claimant upon funds of the insolvent national bank in the hands of a receiver, having in its hands collaterals placed with it at the time it made its loan to the bank by the vice-president of the same, there were several rulings necessary by the peculiar circumstances as they appeared in the case. Among the collaterals to secure this loan was a note for $25,000 made by one party and

when presented, to disallow it, and if an attempt was made to obtain its adjudication, to make such defense as in his judgment was proper. No provision is made by law for the payment of the expenses of the claimant in his litigation beyond the taxable costs, and necessarily that loss must fall on him as it does on every one who has the misfortune to be driven to the courts for the judicial determination of his rights."

[1] Chemical National Bank *v.* Armstrong, (1892) 50 Fed. Rep. 798. SAGE, J., distinguished White *v.* Knox, 111 U. S. 784; s. c., 4 Sup. Ct. Rep. 686, by which the contention of the claimant it was urged was supported, and then said: "In none of the cases decided by the Supreme Court does it appear that any payment on account of the indebtedness of the creditor was made, from the proceeds of collaterals or otherwise, after the suspension of the bank and before the proof of claim. There are two other cases in Pennsylvania, in which the doctrine claimed by counsel for complainant is approved, and the weight of authority is the other way. In Lewis *v.* U. S., 92 U. S. 618; Case *v.* Bank, 100 U. S. 446, and Eastern Township Bank *v.* Vermont Nat. Bank, 22 Fed. Rep. 186, the claim proven was for the entire amount of the principal of the indebtedness as it existed when proved, and at the date of the failure of the bank, for nothing had been realized from collateral, and there had been no partial payments, and the questions as to the time with reference to which the amount due shall be adjusted related exclusively to the payment of interest."

indorsed by a second for the accommodation of the vice-president of the bank. A short time before the maturity of this note and other collaterals, the vice-president of the bank requested that they be not presented for payment, but returned, promising that other collaterals should be substituted for them; all of which was done except that this note was not returned. The insolvent bank did not order back this note, and just afterwards it matured without presentment or notice of dishonor to the indorser, who was the only solvent party to the note. The court held that the claimant national bank, having by its negligence failed to preserve the liability of the indorser, was chargeable with the amount of the note as so much received on its claims. That it was no excuse to the claimant bank that the insolvent bank was not a party to the note, it having received it as a security for a loan to the insolvent bank under circumstances from which it might naturally infer the note to be the property of the insolvent bank. That the objection by the claimant bank that the note was made and indorsed merely for the accommodation of the vice-president, who was not a party to the note, and that consequently the claimant bank could not have recovered thereon if the indorser's liability had been preserved, could not be maintained in view of the fact that the indorser had paid three notes, companions to the one in question, without objection, and of evidence that he was interested with the vice-president in procuring the loan which the note partly secured. That the claimant bank, having refused an offer of the receiver to pay dividends on a fixed sum of money which was about the amount due to it on the loan after deducting collections on collaterals, was not entitled to interest on its dividends on affirmance of the action of the receiver by the court. That on ascertaining the amount on which the bank was entitled to a dividend, money collected on the collaterals after proof of its claim, should not be deducted from the amount proven.[1]

§ 353. Claim of an indorser who paid a note which was not surrendered to him.— In this case a note had been indorsed and discounted at a bank. The bank had placed this note with the clearing house with which it was connected, where it was when the note was about to become due. The indorser paid the amount of this note to the bank which discounted it when it fell

[1] Chemical Nat. Bank *v.* Armstrong, (1892) 50 Fed. Rep. 798.

due, and had a receipt from the cashier for the amount, binding itself to recover the note and return it to the indorser. The bank became insolvent, and a sum in cash largely exceeding the amount paid in by the indorser of this note, which had been placed with the bank's cash, went into the hands of the receiver. The committee of the clearing house having procured a judgment upon this note against the indorser, the latter paid it and brought his action against the receiver of the insolvent bank to recover the money he had paid in to the bank for which this note was to have been surrendered to him. The Circuit Court for the eastern district of Pennsylvania held that the effect of the payment by the indorser to the bank and the giving the receipt by the latter was to establish a fiduciary relation between the parties, and not that of debtor and creditor, entitling the indorser to have the assets in the hands of the receiver applied in payment of the amount he had placed in the bank.[1]

[1] Massey *v.* Fisher, (1894) 62 Fed. Rep. 958. BUTLER, D. J., said: "The money was delivered and received to extinguish the note. Neither party contemplated that the bank might use it for another purpose, leaving the note outstanding, and the plaintiff's liability unextinguished. Such application of it, therefore, would be a violation of duty and a fraud. But the question is not new; it arose and was decided in People *v.* City Bank of Rochester, 96 N. Y. 32. The facts there were substantially like those before us. It is true the check in that case was drawn in terms to pay the note. This, however, is an immaterial difference. It is as plain here, as it was there, that the money was delivered and received to take up the note. In Peak *v.* Ellicott, 30 Kans. 156; s. c., 1 Pac. Rep. 499, the facts were identical with those before us. In each of these cases it was held that the transaction established a fiduciary relation between the parties. * * * The receiver and creditors stand on no higher plane than the bank, and can no more assert that it was the bank's money than the bank could. It is true they are entitled to all the bank's property; but this was not its property. It is not important that the plaintiff's money bore no mark, and cannot be identified. It is sufficient to turn it into the bank's vaults, and find that a sum equal to it (and presumably representing it) continuously remained there until the receiver took it. The modern rules of equity require no more. Knatchbull *v.* Hallett, 13 Ch. Div. 696; National Bank *v.* Insurance Co., 104 U. S. 54; Bank *v.* King, 57 Pa. St. 202; Stoller *v.* Coates, 88 Mo. 514; McLeod *v.* Evans, 66 Wis. 401; s. c., 28 N. W. Rep. 173, 214; People *v.* City Bank of Rochester, 96 N. Y. 32; Bank *v.* Weems, 69 Tex. 489; 6 S. W. Rep. 802; Harrison *v.* Smith, 83 Mo. 210; Beach Eq. Jur. § 285; Fisher *v.* Knight, 61 Fed. Rep. 491; s. c., 9 C. C. A. 582." Bank *v.* Dowd, 38 Fed. Rep. 172, was disregarded. The judge resumed: "There is a class of cases — to which Bank *v.* Beal, 49 Fed. Rep. 606, and Bank *v.* Armstrong, 148 U. S. 50; s. c., 13 Sup. Ct. Rep. 533, belong — in which

§ 354. **Debts due savings banks preferred under New York statutes.**— The Banking Law of New York provides as follows: "Debts due savings banks from insolvent banks preferred. All the property of any bank or trust company which shall become insolvent, shall, after providing for the payment of its circulating notes, if it has any, be applied by the trustees, assignees, or receiver thereof, in the first place, to the payment in full of any sum or sums of money deposited therewith by any savings bank, but not to an amount exceeding that authorized to be so deposited by the provisions of this chapter, and subject to any other preference provided for in the charter of any such trust company."[1] A national bank in the state of New York becoming insolvent, and being placed in the hands of a receiver, there was a submission of a controversy to the Supreme Court of the state of New York as to whether there should not be a judgment in favor of a savings bank of that state against the receiver for the amount of the deposit it had make with the national bank within the limits of the Banking Law, as a preference against the insolvent bank's assets, under the provisions of the law of New York above referred to. The receiver's contention was that the statute of New York was in conflict with sections 5236 and 5242, United States Revised Statutes, which prohibit preferences between creditors of insolvent national banks, and provide for a *pro rata* dividend of assets among the bank's creditors. The Supreme Court of New York held that national banks were subject to state legislation and were governed thereby except where such legislation was in conflict with the act of congress, or where it tended to destroy the utility of said banks as agents of the United States, or interfered with the purposes of the creation; and that it was only when their state law incapacitated them from discharging their duties to the government that it becomes unconstitutional. They upheld the constitutionality of the state law as to the deposit of moneys by savings banks.[2] The court held that this statute of New York as to

it is held that although the relations of the parties there involved were in the beginning fiduciary, they ceased to be so when the agent commingled the money with its own. These, however, were cases where commercial paper was delivered for collection and credit, and where the collection and credit terminated the agency. The commingling and use of the money were in pursuance of the understanding; and upon this construction of the transaction the decisions rest. The distinction is noticed in Knatchbull *v.* Hallett, 13 Ch. Div. 702."

[1] Laws N. Y. 1892, chap. 689, § 130.

[2] Elmira Savings Bank *v.* Davis, (1893) 73 Hun, 357; s. c., 26 N. Y.

savings banks' deposits in insolvent banks, giving them a preference over other creditors, was not in conflict with the statutes of the United States providing for no preference among creditors and for a *pro rata* distribution of the assets of insolvent national banks among the creditors presenting claims to the receivers. And a judgment was rendered in favor of the savings bank against the receiver of this national bank for the amount of its deposits.[1] Whether or

Supp. 200. The court referred to and quoted from Waite *v.* Dowley, 94 U. S. 527; National Bank *v.* Commonwealth, 9 Wall. 353, and W. U. Tel. Co. *v.* Massachusetts, 125 U. S. 551, and said: "Applying these principles to the present case, it is difficult to see how the state act interferes with the utility of the national bank as an agent or instrumentality of the general government. No possessory right is given until after the bank, by reason of its insolvency, has ceased to be of any utility as an agent or instrumentality of the government, and after its circulating notes are provided for. The logic of the case in 9 Wallace will uphold the law in question here unless it is in conflict with some provision of the United States statute on the subject."

[1] Elmira Savings Bank *v.* Davis, (1893) 73 Hun, 357; s. c., 26 N. Y. Supp. 200. The court referred to the application of the ordinary doctrine of set-off in case of insolvency against the receiver of a national bank in Scott *v.* Armstrong, 146 U. S. 499, and then said: "In Casey, Receiver, *v.* La Société de Credit Mobilier, 2 Woods, 77, it was held that the preference of one creditor by a national bank, mentioned in section 5242 of the Revised Statutes, is a preference given to the creditor to secure or pay a pre-existing debt; that when a national bank receives a loan on condition that the lender shall be secured therefor, and security is accordingly given by pledging a part of the assets of the bank, this is not a preference within the meaning of section 5242, although the bank is then in an embarrassed state; that the fact that the assets pledged were changed from time to time as they fell due, and others substituted in their stead, according to the contract between the bank and the pledgee, did not make the pledge of the substituted assets void; that the title of the receiver is the same as that of an assignee in bankruptcy, and is subject to all equities. * * * In the present case it must be presumed that the national bank, when, from time to time it received the deposits from the savings bank, knew of the law which authorized such deposit and provided for the preference. The savings bank was not bound to deposit in that particular bank, nor was the latter bound to receive the deposit. But if the one made and the other received the deposit, it must be assumed that both parties then intended that the security provided for by the statute should, at the proper time, be operative. There was then, in effect, a contract that if the deposit or loan was made, the security should be given. This was a part of the transaction in each case of deposit. It was not a case of a security for a prior indebtedness, but it was a case where, on each occasion, a consideration passed of equal value with the security or right given. In this view, and within the rulings in the cases above referred to, there was not a preference in violation of the provisions of section 5242. By virtue of the state act and the conduct of the parties, the savings bank had at least an equitable lien, which is effective

not a savings bank, under the statutes of New York, would be entitled to a preference or be bound by the United States statute to take its *pro rata* part of the proceeds of the assets of an insolvent national bank, does not appear to have been yet passed upon by the federal courts. But it will probably be very soon. A suit of a savings bank against a receiver of a national bank instituted in the courts of New York has been removed to the United States Circuit Court for the northern district of that state. There was a motion made in the federal court to remand the case, but the court denied the motion.[1] A motion to remand this suit to the state court from which it had been removed to the federal court on the ground that it was not a suit "arising under the Constitution or laws of the United States" under the act for removal of cases from the state courts, was denied.[2]

within the principles laid down in Scott *v.* Armstrong, and is not antagonistic to the *pro rata* distribution provided for in section 5236. The receiver took, subject to any valid liens or equities. The bank that he represents received the deposits subject to the condition imposed by the state statute, and whether it be said that a trust was impressed or a lien imposed, the statute bound the bank and its assets when they passed to the receiver and interfered with no rights of the government. The principles laid down in the Scott case are quite applicable, and justify the claim of plaintiff to a preference."

[1] Auburn Sav. Bank *v.* Hayes, (1894) 61 Fed. Rep. 911. Cox, D. J., said: "This, it seems to me, is a controversy 'arising under the laws of the United States.' Were it not for the state law the plaintiff would of course be paid ratably with the other creditors. Whether or not the state can legislate in this manner with reference to national banks is a question which the federal courts and not the state courts should decide. To give the state courts sole jurisdiction to determine whether state legislation is in conflict with the National Bank Act would, to say the least, tend to throw the national system into confusion. The doctrine of Tehan *v.* Bank, 39 Fed. Rep. 577, is hardly applicable to the present cause. In the Isham case there was no federal question, because the rule of the common law applicable to that controversy was controlling alike upon the state and United States courts. Here, on the contrary, the construction of a United States statute is involved. The plaintiff may be right as to the interpretation of the statute, but that its construction is involved there can be no doubt. Whatever defense the defendant has depends upon the sections [of the United States Revised Statutes] referred to. The question presented by the motion is not what the construction of these sections should be, but whether the state courts or the United States courts should construe them. I am of the opinion that this power belongs to the United States courts. Sowles *v.* Witters, 43 Fed. Rep. 700; Grant *v.* Bank, 47 Fed. Rep. 673; Walker *v.* Richards, 55 Fed. Rep. 129."

[2] Hot Springs Independent School Dist. No. 10 of Fall River County *v.* First Nat. Bank of Hot Springs, (1894) 61 Fed. Rep. 417. SANBORN, Circuit

§ 355. Claims of municipal corporations for moneys deposited by their officers.— The treasurer and tax collector of a county in California, without authority of law, deposited county moneys in a bank and received certificates of deposit marked "Special." In an action in equity brought by the county, the bank having become insolvent, it was held in the United States Circuit Court for that district that the title to the moneys did not pass to the bank, although there was no agreement that the identical bills should be returned, and they were mixed with the bank's general fund, and the county was entitled to recover an equal amount from the receiver prior to the payment of the general depositors. Upon the question raised on behalf of the receiver that there was no jurisdiction of the case in an equity court, the plaintiff having his remedy at law, it was held that the county's rights in such case were enforceable only by a bill in equity, there being no priority of contract between it and the bank.[1] The United States Circuit Court for the district of

Judge, said: "This suit is brought to compel the receiver of this insolvent national bank to first pay to the complainant, out of the funds of the bank in his hands, several thousand dollars before he pays any dividend to any creditor, on the ground that this receiver holds this sum of money as a trust fund for the complainant, and not as part of the property of the bank, to be distributed among its creditors. Whatever funds and property this receiver has he has received from this insolvent bank, and he holds them by virtue of the laws of the United States under which he holds his appointment, and in accordance with which he must discharge the trust devolved upon him. In this suit he has interposed a demurrer to the plea of the complainant, and the question now at issue is, what construction shall be placed upon the provisions of the National Banking Law with reference to the distribution of the funds of the insolvent banks by receivers under the admitted facts of this case? I am clearly of the opinion that this case is one arising under the laws of the United States. * * * Sowles *v.* Witters, 43 Fed. Rep. 700; Sowles *v.* Bank, 46 Fed. Rep. 513; San Diego Co. *v.* California Nat. Bank, 52 Fed. Rep. 59."

[1] San Diego County *v.* California Nat. Bank, (1892) 52 Fed. Rep. 59. It was said by the court: "A similar point was raised in the case of National Bank *v.* Insurance Co., 104 U. S. 54. In that case one Dillon was the agent of the insurance company. He kept an account with the bank; the account was entered on the bank books with him as general agent. As agent of the insurance company he collected, and it was his duty to remit, the premiums. In the course of his dealings with the bank he borrowed money on his personal obligations. Finally the bank sought to appropriate his deposits to the payment of this debt. The insurance company filed its bill in equity to recover the amount of those deposits, as equitably belonging to it. The fact that they were premiums received for

Washington denied an injunction upon the motion of a county of that state to forbid the receiver of a national bank paying dividends to creditors pending a suit by the county to recover of the receiver the amount of moneys deposited in the bank on its account by the treasurer of the county. The right to priority over other creditors of the bank was claimed by the county on the ground that the officers of the bank, at the time of accepting the deposit, knew that the money was in the official custody of the treasurer, and, therefore, a trust fund. It was held by the court that under the provisions of United States Revised Statutes (§ 5242), which forbids all preferences among creditors, the county had no priority.[1] Cotemporaneously with this last-referred-

the insurance company was shown. The court said: 'It is objected that the remedy of the complainant below, if any existed, is at law, and not in equity. But the contract created by the dealings in a bank account is between the depositor and the bank alone, without reference to the beneficial ownership of the moneys deposited. No one can sue at law for a breach of that contract except the parties to it. There was no privity created by it, even upon the facts of the present case, as we have found them between the bank and the insurance company. The latter would not have been liable for an overdraft by Dillon, as was decided by this court in National Bank *v.* Insurance Co., 103 U. S. 783; and, conversely, for the balance due from the bank no action at law upon the account could be maintained by the insurance company. But although the relation between the bank and its depositors is that merely of debtor and creditor, and the balance due on the account is only a debt, yet the question is always upon 'To whom in equity does it beneficially belong?' If the money deposited belongs to a third person, and was held by the depositor in a fiduciary capacity, its character is not changed by being placed to his credit in his bank account.' See, also, Bank *v.* Gillespie, 137 U. S. 411; s. c., 11 Sup. Ct. Rep. 118; Bank *v.* Walker, 130 U. S. 267; s. c., 9 Sup. Ct. Rep. 519. In the present case not only did the defendant bank, according to the averments of the bill, have knowledge that the depositors of the moneys in question were, at the time of such deposits, officers of the complainant county, and that the moneys so deposited belonged to the complainant, and were, therefore, held by the officers depositing the same in trust for the county, but the bank is chargeable with notice of the fact that the law of the state made it illegal for those officers to make, or the bank to receive, such deposits. Yarnell *v.* City of Los Angeles, 87 Cal. 603; s. c., 25 Pac. Rep. 767." As to the rule declared in the text, see National Bank *v.* Insurance Co., 104 U. S. 56, 67; Peters *v.* Bain, 133 U. S. 694; s. c., 10 Sup. Ct. Rep. 354.

[1] Spokane County *v.* Clark, (1894) 61 Fed. Rep. 538. The court, as to the law in such cases, said: "Money held by a bank as trustee is not a part of its assets, nor legally subject to claims of its creditors. If the money had been kept intact as a special deposit, or if it were possible to prove that any of the complainant's money or any securities or property acquired by the

to case, the United States Circuit Court for the district of Oregon held adversely to the claim of a county of Oregon in a suit against the receiver of a national bank, and the intervention in the same suit of a city of that state, which sought to have a decree that certain deposits made in the bank by the sheriff of the county and the treasurer of the city to be property of the county and city respectively, and that the receiver hold the same as trustee for these municipalities, and that they have a lien upon all money, choses in action and other property of the bank to the amount of the aggregate of the deposits made by their officials. They were held not to have any preference over other creditors.[1]

bank by investment of money with which it had been mingled came into the receiver's hands, according to principles of equity now firmly established, the rights of this complainant to the relief prayed for would be clear; but there is no averment in the bill of complaint that the money deposited can be traced, nor that the estate which has come into the receiver's hands includes securities or property of the bank acquired since receiving said deposit. It does not appear that any of said money was invested, nor that it was not all paid out to the depositors or creditors before the bank closed its doors. The complainant's argument is based upon an assumption that the bank profited by tortiously converting the money. That the bank could not acquire title to money of the county by its own wrongful act is manifestly true; but where the holder of trust funds has actually expended the same, and become insolvent, a practical difficulty in the way of restoring the money to its owner arises, which can no more be overcome by a court of equity than by any other human agency. That very difficulty confronts the complainant and the court in this case; for it is a fact that, in place of actual money in the bank when it suspended, there was only a legal liability, arising from the conversion and expenditure of the money deposited by the treasurer. The practical difficulty of the case is not diminished in the least by characterizing the conversion as a tort, or by any stronger term, for the fact remains that the money is gone. It cannot be recovered until found. The plaintiff's right in this suit attaches not to specific property to which it has title, but only to a chose in action. The law forbids preferences in the distribution of the estate of an insolvent national bank among its creditors, and makes no exceptions of debts due to municipal, county or state governments, nor in favor of claims arising *ex delicto.*" The court refers to National Bank *v.* Insurance Co., 104 U. S. 54; Peters *v.* Bain, 133 U. S. 670; s. c., 10 Sup. Ct. Rep. 354; Frelinghuysen *v.* Nugent, 36 Fed. Rep. 229; Bank *v.* Armstrong, 148 U. S. 50; s. c., 13 Sup. Ct. Rep. 533, as sustaining its holding.

[1] Multnomah County *v.* Oregon Nat. Bank, (1894) 61 Fed. Rep. 912. BELLINGER, D. J., *arguendo*, said: "It is settled that a person may follow and reclaim his property, wrongfully appropriated by another, so long as he can find it. If its form has been changed, he may follow the substantial equivalent of his property in whatever form. The property into which his own has been changed is impressed with a trust in his favor.

§ 356. Claims preferred to those of general creditors — illustrations.— In a late case before the Court of Civil Appeals in Texas, the facts were that plaintiff sent a draft to the bank for collection. The bank collected it and then passed into the hands of a receiver without remitting. The defense of the receiver to the action of the plaintiff was that plaintiff had sent the draft for

But the great weight of authority is against any extension of the rule beyond this. The cases most relied upon by the complainants were those in the Supreme Court of Wisconsin, but since the argument defendant has called my attention to the case of Silk Co. *v.* Flanders, (decided in the Supreme Court of Wisconsin in March of this year) 58 N. W. Rep. 383, which overrules former decisions upon this question, and declares the doctrine that when trust money becomes so mixed up with the trustee's individual fund that it is impossible to trace and identify it as entering into some specific property, the trust ceases; that the court will go as far as it can in thus tracing and following trust money, but when, as a matter of fact, it cannot be traced, the equitable right of the *cestui que trust* to follow it fails. The recent cases of Slater *v.* Oriental Mills, (by the Supreme Court of Rhode Island) 27 Atl. Rep. 443, and Association *v.* Austin, (Supreme Court of Alabama) 13 So. Rep. 908, are to the same effect. The case of Shields *v.* Thomas, (Supreme Court of Mississippi) 14 So. Rep. 84, is similar to the present case in its facts. The sheriff of a county, without authority, deposited in a bank, which shortly afterwards failed, taxes collected by him, the officers of the bank knowing the character of the fund. The cash that came into the hands of the receiver of such bank was less than the amount of such fund, and it did not appear that the fund, or any part of it, came into the receiver's hands, either in its original form or as a part of the mass of the bank's assets. The court refused to make the payment of such fund out of the assets in the receiver's hands, a charge upon such assets precedent to the claims of the other creditors of the bank. These are all recent and well-considered cases, and each of these contains a large number of citations in support of the conclusion reached." The court then referred to the following case against these authorities, to wit: San Diego County *v.* California Nat. Bank, 52 Fed. Rep. 59, in which Ross, J., said: "The ordinary creditors became such voluntarily. They deposited the money with the bank with their eyes open. But the money of the complainant was deposited by its officers and received by the bank, not only without the knowledge of the complainant, but contrary to law. To put the complainant on the same terms with the ordinary creditor is to make the former share in a loss to which it did not voluntarily subject itself, and to give to the latter a share in money which never in equity became the property of the bank. This is certainly not just." BELLINGER, D. J., disapproved of this in these words: "Notwithstanding the respect in which I hold the opinion of Judge Ross, I cannot adopt this view in the face of the cases that hold this other doctrine. The correctness of his conclusions as to the injustice of giving the general creditors of the bank a share in the money which never in equity became the property of the bank, cannot be questioned. But this is not what happens in the case under consideration. It does not appear that the money for distribution in-

collection merely, and without other instructions, and that the relation between plaintiff and the bank with reference to the collection was that of creditor and debtor, and that, therefore, the plaintiff was not entitled to the relief sought. The court held that the bank was his trustee, not his debtor, and that he was entitled to be paid the amount of the collection.[1] A Nebraska bank had been impounded under the state banking laws and was in the hands of a receiver within the jurisdiction of the Supreme Court of the state. The receiver declined to pay a certain claim,

cludes any part of that belonging to the involuntary creditor. If this did appear, the lien of such creditor would attach, and he would have his preference. The fact that the money of such creditor or *cestui que trust* cannot be turned to the fund sought to be charged, is the reason that the preference is refused. If his money has been paid out, or has otherwise disappeared, it would not be just that he should take to the exclusion of the general creditors of the bank, who are in no way responsible for the bank's delinquency, and whose deposits may comprise the entire fund which such creditor seeks to appropriate to his exclusive use. His so-called right of preference, in other words, cannot, in justice, extend to the property of others. The theory of preference does not apply in these cases. There is no preference by reason of an unlawful conversion. The so-called right to be preferred in the case of a wrongful conversion is a right of ownership — a right of property; a right which lays hold of the property whether in its original or in a substituted form; a right which follows the property so long as it can be ascertained to be the same property, or its product, and only does so because the property to be reached can be ascertained to be the same property, or its product. When the means of ascertainment of the identity of property or proceeds fails, the right fails."

[1] Hunt *v.* Townsend, (Tex. 1894) 26 S. W. Rep. 310. It was said by James, Ch. J., after stating the words of the instruction to the bank: "The testimony discloses, in addition to this, that this bank had previously made similar collections for the plaintiff, and that in no instance was the collection carried to plaintiff's credit, as depositor, by the bank, but the entries were confined to a collection register, and remittances made promptly without further communications. It appears that the proceeds of this collection were not remitted, and became mingled with the general funds of the bank, and that more than the amount thereof was on hand of such funds when the property of the bank passed into the hands of the receiver. It is clear to my mind from the discussion of this subject in Bank *v.* Weems, 69 Tex. 489; s. c., 6 S. W. Rep. 802, that the facts will admit of no other conclusion than the one reached by the district judge. The course of dealing between these parties and the acts of the banks in reference to such transactions, necessarily involved an understanding that the collection should be made and remitted without unreasonable delay. There is nothing from which could be implied an authority for the bank to hold the money, and treat it as a deposit. The amount of this collection was on hand of the general funds of the bank when the receiver took possession, and plaintiff is entitled to receive the same, instead of a *pro rata* with creditors."

and the matter, upon his application to the court for direction, was referred to a referee. This referee found that on a certain date the bank made and delivered to claimant its twelve certificates of deposit of $375 each, aggregating $4,500, due and payable, the first, one month, and the others at intervals of one month each thereafter; all drawing interest at six per centum per annum. That the bank paid the first four of said certificates of deposit on the receipt of same by the bank in the usual course of business, and that claimant was the holder and owner of the remaining eight certificates of deposit, and that the same were due and wholly unpaid. That the certificates of deposit were presented to the bank, or the receiver, at their maturity, and payment demanded and refused for want of funds or from want of an order of court directing payment. That the consideration for the issuance of the certificate of deposit was two certain notes and mortgages of a par value of $5,000, several unsecured small notes of a par value of about $1,000, and a small balance on deposit with the bank. That the sale of these securities was made by the claimant in person and on the faith of the solvency of the bank with which he dealt, through its president. That these certificates of deposit were never entered as a charge or liability of the bank on its books, but of this claimant had no knowledge until long after the issuance thereof, but had reason to believe, and did believe, that such certificates represented a *bona fide* indebtedness of the bank to the owner of such certificates. That at the time the certificates of deposit were issued, claimant had no knowledge of the insolvency of the bank issuing them, but took them in the ordinary course of business, in good faith, relying on the solvency of the bank and the *bona fides* of the whole transaction. His conclusion of law was that the amounts due upon the face of the unpaid certificates of deposit were due with interest to the claimant from the bank, and that the receiver should enter for payment and pay the same as other claims not contested. There were exceptions to the report of the referee, but upon a full consideration of the findings and other evidence commented upon as confirming the propriety and justice of the report of the referee, the Supreme Court overruled the exceptions and confirmed the report.[1] In a case where a Texas bank had been placed in the hands of a receiver, the bank being declared insolvent, the agreed statement

[1] State *v.* Farmers & Drovers' Bank of Battle Creek, (1893) 36 Neb. 675.

of facts showed "that in the course of dealing between the [Texas bank] and a [New York bank] the latter was in the habit of discounting notes for the [former] and of forwarding the same on maturity to the [former] for collection and return, with an understanding that the proceeds of such discount notes should be preserved by the [Texas bank] as the property of the [New York bank] and returned to it as such." One question to be determined by the Supreme Court of Texas was, whether, under the agreement and the course of dealing between the two, the collecting bank was to be decreed the trustee of the funds received by it upon the notes which were paid, and of the renewed obligations which were taken in lieu of those which were not paid. The court, upon this question, said: "We think the facts stated in the agreed statement settle the question of trust in the affirmative. If the securities had been sent for collection merely, the proceeds to be credited to the New York bank, it is clear that after their collection the relation of debtor and creditor would have subsisted, and the latter would have no claim upon the funds. But, by the understanding between the banks and the actual transactions between the parties, as shown by the agreed evidence, a special agency was created, and the [Texas bank] had no authority to hold and credit the proceeds of the notes, but was bound to remit them immediately to its correspondent."[1] As to the claim of the New York bank for full payment of the notes renewed and discounted by it, the court said: "[It] stands upon a very different ground. The agreed evidence shows that the renewed obligations were indorsed by the [Texas bank] and deposited as collaterals with banking houses in the city of New York, and were paid to the holders either in

[1] Continental National Bank of New York *v.* Weems, Receiver, (1888) 69 Tex. 489; s. c., 6 S. W. Rep. 802. The court said: "This principle was clearly recognized by this court in the case of The City Bank of Sherman *v.* Weiss, 67 Tex. 331, and is sustained by the great weight of authority, as appears from the citations in the opinion. But it is insisted by counsel for the [receiver] that there is other evidence in the record not inconsistent with the agreement, which shows that the relation of debtor and creditor and not that of trustee and *cestui que trust* was created by the transaction. We think, however, that any evidence to show this fact in the face of the explicit statement in the admitted proof would be inconsistent with the agreement, and should have been disregarded by the court, whether objected to or not. But we do not regard the evidence relied on as being in conflict with that in the agreed statement."

whole or in part. As to the one which was only partially paid, the agreement recites 'that said renewal note to the amount of twelve hundred and fifty dollars went to pay the draft of said [insolvent bank], and benefited its estate accordingly.' As to the other two, the language in reference to the disposal of the proceeds is a little different, but we presume it means the same thing. We, therefore, deduce from the admitted facts that with the proceeds of the notes now under consideration, obligations of the insolvent bank were discharged, and that no other benefit accrued to its estate. Now, the question is, has the [New York bank] a lien upon the general assets in the hands of the receiver for the proceeds so appropriated? We think not. To hold the affirmative of this proposition would be to declare that every one who receives the money of another in a fiduciary capacity and expends it in the payment of his own debts, thereby creates a lien upon his entire estate in favor of the owner of the money so expended. But this is clearly contrary to the doctrine of constructive trusts. The true rule is that the trust estate must be clearly turned into other specific property in order that the *cestui que trust* may claim either the property itself or a lien upon it. This is the doctrine uniformly applied in the older cases and laid down by the text books upon the law of trusts."[1] In this same case the courts in which the proceedings in insolvency of the Texas bank were had, had charged the New York bank with certain notes sent by the former to the latter to be discounted. The facts in the case were that the Texas bank sent the notes to the New York bank to be discounted and to have the proceeds placed to its credit, according to a previous course of dealing between them. The latter refused to discount the paper, and so notified its correspondent, but before the notice of refusal to discount was received by the latter, not doubting that the paper would be discounted, it drew upon the New York bank to the amount of about $5,000. The New York bank paid the drafts, relying upon the notes for reimbursement. Of the contention that the New

[1] Continental National Bank of New York *v.* Weems, Receiver, (1888) 69 Tex. 489, 498, 499; s. c., 6 S. W. Rep. 802; citing Perry *v.* Phelips, 4 Ves. 107; Lewis *v.* Madocks, 17 Ves. 48; Denton *v.* Davies, 18 Ves. 499; Taylor *v.* Plumer, 3 Maule & S. 562; Pennell *v.* Deffell, 4 De G., M. & G. 372; Knatchbull *v.* Hallett, 13 Ch. Div. 696; Pharis *v.* Leachman, 20 Ala. 662; Noble *v.* Andrews, 37 Conn. 346; Roberts *v.* Broom, 1 Harvey, 57; 2 Perry on Trusts, § 835 *et seq.;* 2 Story's Eq. Jur. § 1258; 2 Pomeroy's Eq. § 1051.

York bank had a lien upon this paper for the payment not only of the $5,000 so paid, but also for its general balance on account against its correspondent, the Texas Supreme Court said: "This proposition cannot be maintained. It is frequently said that a banker has a lien upon the funds in his hands for the indebtedness of his creditors, and it is argued that the rule applies unless there is an agreement to the contrary. But we understand the rule to be that in order to give such lien there must be a contract for that purpose, either express or implied. 'The credit must be given on the credit of the securities or valuables either in possession or expectancy. Russell *v.* Hadduck, 3 Gilm. 233. This is the extent of the banker's lien.' Fourth Nat. Bank *v.* City Nat. Bank, 68 Ill. 398. See, also, Jarvis *v.* Rogers, 15 Mass. 389; Lucas *v.* Dorrien, 7 Taunt. 279. In the case last cited, a bond was presented to a banker by his customer as collateral for a loan, which the banker declined to accept, and it was casually left with him. It was held that he had no lien upon it. So, in this case, the [New York bank] having refused the paper, had no right to hold it, and should have returned it. Having failed to do so it has no lien except for the amount of the drafts paid after the paper was received."[1] An Ohio national bank entered into a contract with a Pennsylvania bank to do the collection business of the latter in western cities, by itself or through its agents, and to allow a percentum upon daily balances, and to remit on the first, eleventh and twenty-first of each month. The Pennsylvania bank stamped upon its paper forwarded for collection, "Pay to" the Ohio bank "or order for collection per" the Pennsylvania bank. The Ohio bank became insolvent and was placed in the hands of a receiver. Collections had been made on paper of the Pennsylvania bank and the latter brought its action against the receiver to recover, as special funds belonging to it at the time of the insolvency of the Ohio bank, the various amounts collected on its paper forwarded for collection. There was an appeal from the United States Circuit Court to the Supreme Court of the United States. The United States Supreme Court

[1] Continental National Bank of New York *v.* Weems, Receiver, (1888) 69 Tex. 489, 501; s. c., 6 S. W. Rep. 802, where the court stated that the proper judgment would have been to charge the New York bank in the account with the moneys collected upon the paper, and with the value of so much of it as remained unpaid, to be set off by the amount of the drafts drawn upon it by the Texas bank after the notes were forwarded for discount.

held that the Pennsylvania bank was entitled to have the amounts collected by the sub-agents of the Ohio bank and paid by them to the receiver of the latter, paid to it out of the assets in his hands.[1] As to those moneys collected by the sub-agents to which the Ohio bank was in debt, and which collections had been credited by the

[1] Commercial Bank of Pennsylvania *v.* Armstrong, (1893) 148 U. S. 50. Mr. Justice BREWER, speaking for the court, said: "We agree with the circuit judge, that the relation created between the banks as to uncollected paper was that of principal and agent, and that the mere fact that a sub-agent of the [Ohio] bank had collected the money due on such paper, was not a mingling of those collections with the general fund of the [Ohio bank], and did not operate to relieve them from the trust obligation created by the agency of the [Ohio bank], or create any difficulty in specially tracing them. As to such paper, the transaction may be described thus: The plaintiff handed it to the [Ohio bank], the [latter] handed it to a sub-agent, the agent collected it, and held the specific money in hand to be delivered to the [Ohio bank]; then the failure of the [latter] came, and the specific money was handed to its receiver. That money never became a part of the general fund of the [Ohio bank]; it was not applied by the sub-agent to reducing the indebtedness of the [Ohio bank] to it, but it was held as a sum collected to be paid over to the [latter], or to whomsoever might be entitled to it. The [Ohio bank] received the paper as agent, and the indorsement 'for collection' was notice that its possession was that of agent and not of owner. In Sweeny *v.* Easter, 1 Wall, 166, 173, in which there was an indorsement 'for collection,' Mr. Justice MILLER said: 'The words 'for collection' evidently had a meaning. That meaning was intended to limit the effect which would have been given to the indorsement without them, and warned the party that, contrary to the purpose of a general or blank indorsement, this was not intended to transfer the ownership of the note or its proceeds.' And in White *v.* National Bank, 102 U. S. 658, 661, where the indorsement was 'for account,' the same justice, speaking of the indorsement, said: 'It does not purport to transfer the title of the paper, or the ownership of the money when received.' The plaintiff, then, as principal, could unquestionably have controlled the paper at any time before its payment, and this control extended to such time as the money was received by its agent, the [Ohio bank]. Butchers', etc., Bank *v.* Hubbell, 117 N. Y. 384; Manufacturers' Bank *v.* Continental Bank, 148 Mass. 553; Freeman's Bank *v.* National Tube Works, 151 Mass. 413; Armstrong *v.* National Bank of Boyertown, (Ky.) 14 S. W. Rep. 411; Crown Point National Bank *v.* Richmond National Bank, 76 Ind. 561. In those cases the suits were against sub-agent banks. It is true that in most of them the collection was made by the sub-agent after the avowed insolvency of the agent, but that fact, we cannot think, is decisive. If, before the sub-agent parts with the money or credits it upon an indebtedness of the agent bank to it, the insolvency of the latter is disclosed, it ought not to place the funds which it has collected, and which it knows belong to a third party, in the hands of that insolvent agent or its assignee; and, on the other hand, such insolvent agent has no equity in claiming that this money, which it has not yet received, and which belongs to its principal, should be transferred to

sub-agents upon the debts of the Ohio bank to them before its insolvency was disclosed, the court held that the moneys had practically passed into the hands of the Ohio bank, and the collection had been fully completed; that it was the same as though the money had actually reached the vaults of the latter; and, so far as these moneys were concerned, there was no trust attached to them; the Ohio bank was, as to them, simply a debtor to the Pennsylvania bank.[7] In a Nebraska case for the foreclosure of a

and mixed with its general funds in the hands of its assignee, for the benefit of its general creditors, and to the exclusion of the principal for whom it was collected. Whether it be said that such funds are specifically traceable in the possession of the sub-agent, or that the agent has never reduced those funds to possession, or put itself in a position where it could rightfully claim that it has changed the relation of agent to that of debtor, the result is the same. The [Ohio bank] received this paper as agent. At the time of its insolvency, when its right to continue in business ceased, it had not fully performed its duties as agent and collector; it had not received the moneys collected by its sub-agent. They were traceable as separate and specific funds, and, therefore, the plaintiff was entitled to have them paid out of the assets in the hands of the receiver, for when he collected them from these sub-agents he was in fact collecting them as the agent of the principal. No mere bookkeeping between the [Ohio bank] and its sub-agent could change the actual status of the parties, or destroy rights which arise out of the real facts of the transaction."

[1] Commercial Bank of Pennsylvania *v.* Armstrong, (1893) 148 U. S. 50. Mr. Justice BREWER said: "The conclusions of the Circuit Court [upon this branch of the case] were based upon the idea that these collections could not be traced, because they had passed into the general fund of the bank. We think, however, a more satisfactory reason is found in the fact that, by the terms of the arrangement between the plaintiff and the [Ohio bank], the relation of debtor and creditor was created when the collections were fully made. The agreement was to collect at par, and remit the first, eleventh, and twenty-first of each month. Collections intermediate these dates were, by the custom of banks and the evident understanding of the parties, to be mingled with the general funds of the [Ohio bank] and used in its business. The fact that the intervals between the dates and remitting were brief is immaterial. The principle is the same as if the [Ohio bank] was to remit only once every six months. It was the contemplation of the parties, and must be so adjudged according to the ordinary custom of banking, that these collections were not to be placed on special deposit and held until the day of remitting. The very fact that collections were to be made at par shows that the compensation for the trouble and expense of collection was understood to be the temporary deposit of the funds thus collected, and the temporary use thereof by the [Ohio bank]. The case of Marine Bank *v.* Fulton Bank, 2 Wall. 252, is in point, though it may be conceded that the facts in that, tending to show the relation of debtor and creditor, are more significant than those here. In the spring of 1861, the Fulton Bank of New York sent two notes for collection to the

mortgage upon real estate of a husband and wife, it appeared that the husband was president of a bank to which the owner of certain notes and mortgages had sent directly with instructions to collect the amounts due in each instance, and remit to him, etc. The bank did collect and remit, as instructed, the most of the notes and mortgages. The president of the bank collected himself the amounts due on the others, and not remitting, afterwards, with his wife, executed the mortgages involved in this action to secure the amounts to the plaintiff, who was the owner of the notes and mortgages. The bank being insolvent had passed into the hands of a receiver, and it was claimed before the court that the mortgages were to secure the debt of the president to the bank for the moneys collected, and that the moneys realized out of these mortgages should go into the general funds of the bank in the hands of the receiver, and that there should be no preference of this creditor as to that fund. It was found by the trial court that the

Marine Bank of Chicago; there being some trouble about currency, the Fulton Bank requested the Marine Bank to hold the avails of the collection subject to order, and advise amount credited. Afterwards the Marine Bank sought to pay in the currency which it had received on the collection, then largely depreciated, but its claim in this respect was denied, Mr. Justice MILLER, speaking for the court, saying: 'The truth, undoubtedly, is * * * that both parties understood that when the money was collected plaintiff was to have credit with the defendant for the amount of the collection, and that defendant would use the money in its business. Thus the defendant was guilty of no wrong in using the money because it had become its owner. It was used by the bank in the same manner that it used the money deposited with it that day by its city customers; and the relation between the two banks was the same as that between the Chicago bank and its city depositors. It would be a waste of argument to attempt to prove that this was a debtor and creditor relation. All deposits made with bankers may be divided into two classes, namely, those in which the bank becomes bailee of the depositor, the title to the thing deposited remaining with the latter; and that other kind of deposit of money peculiar to banking business in which the depositor, for his own convenience, parts with the title to his money and loans it to the banker, and the latter, in consideration of the loan of the money and the right to use it for his own profit, agrees to refund the same amount or any part thereof on demand. The case before us is not of the former class. It must be of the latter.' That reasoning is applicable here. Bearing in mind the custom of banks, it cannot be that the parties understood that the collections made by the [Ohio bank] during the interval between the days of remitting were to be made special deposits, but, on the contrary, it is clear that they intended that the moneys thus received should pass into the general funds of the bank and be used by it as other funds, and that when the day for remitting came the remittance should be made out of such general funds."

sum claimed, the amount of plaintiff's notes collected, was due to him, and that he was entitled to a foreclosure against certain of the lots of land mortgaged; and that, as to those lots, the mortgage gave a lien to the plaintiff for the amount of the mortgage thereon, and that the execution of such mortgage did not confer or pass any right or title to said lots to the receiver of the bank. The Supreme Court affirmed the judgment upon these findings.[1]

§ 357. Claims not preferred to those of general creditors — illustrations.— The owner of a note executed by a depositor in a Michigan bank sent the same to the bank for collection. At the time it fell due the maker having to his credit in the bank, as appeared on its books, more than sufficient to meet the note, gave his check for the amount, and the note was delivered to him by the bank. Within ten days afterwards the bank's insolvency was declared, and its affairs placed in the hands of a receiver. It appeared that there was not, at the time the check of the maker of the note was drawn, cash to any amount in the bank, it being then in an insolvent condition, and the receiver had placed

[1] Griffin *v.* Chase, (1893) 36 Neb. 328. The reasoning and statement of law involving the rights of the parties in the case were as follows: "We think that the proof establishes the fact that the bank received the money in question of the plaintiff, as his agent, with directions to remit to him. The money was not to be deposited in the bank but sent at once. This simplifies the case very much. It is very clear that the bank was the agent of the plaintiff, and that the relation of principal and agent existed between them. The bank, therefore, held the funds of the plaintiff as trust funds, and they were never mingled with the funds of the bank with the plaintiff's consent. In Peak *v.* Ellicott, 30 Kans. 156, where a party had paid to the receiver of a bank the amount of a note given by him to the bank, which the cashier claimed had been re-discounted in another town, but would be sent for and canceled, the bank soon afterwards failed without canceling the note. The court held that the money so received was a trust fund which must be applied to the purposes indicated, and that it did not become a part of the assets of the bank. To the same effect, Ellicott *v.* Barnes, 31 Kans. 170. In McLeod *v.* Evans, 66 Wis. 401; s. c., 28 N. W. Rep. 173, it was held that a banker who accepts for collection a draft and, in fact, collects the money thereon, holds the same as trustee of the owner; and, after his assignment for the benefit of creditors, the trust character still adheres to the funds in the hands of the assignee irrespective of other creditors. Francis *v.* Evans, 69 Wis. 115; s. c., 33 N. W. Rep. 93; Anheuser-Busch Brewing Assn. *v.* Morris, 36 Neb. 31. Other cases to the same effect can readily be cited, but it is unnecessary. That the moneys were held in trust there is no doubt, and as such they did not belong to the bank or become a part of its assets."

in his hands but a nominal sum in cash. The owner of the note petitioned the court appointing and controlling this receiver to order him to pay the amount which was apparently collected for him by the bank. He insisted that the acceptance of the check by the cashier in payment of the note, as stated, was the same in effect as though the money had been actually paid into his hands by the maker of the same, and by the cashier put into the funds of the bank for the benefit of the general creditors, or traced into the hands of the receiver, thus giving the petitioner the right to claim that in equity the amount of money claimed should be considered as a trust fund in the hands of the receiver, which should be paid to the petitioner by him in full, and without regard to the claims of the other creditors of the bank. The contention on behalf of the receiver was that the relation of trustee and *cestui que trust* as to this amount did not exist, based upon the fact that there was no payment of money for the note by the maker of the same; that, as a matter of fact, in consequence of the insolvent condition of the bank on the day he gave his check in payment of the note he had no money on deposit, but only a credit on account of the deposits which he had made at different times before that date. The prayer of the petitioner was denied, and the Supreme Court of Michigan affirmed this judgment on the appeal.[1] Here two banks for several years had

[1] Sherwood *v.* Milford State Bank, (1892) 94 Mich. 78. The opinion of the court in the matter was thus expressed: "If the bank had been paid the money for the note, or if, having taken the check as it did, it had taken the money which it represented, and in either case converted it into any other fund or other assets, and it could have been traced into the hands of the receiver by the petitioners, their right to the order asked for would be clear under the general rule that, when property held upon trust to keep, use, disburse or invest in any particular manner is misapplied by the trustee, and converted into different property or sold, and the proceeds thus misapplied, the property may be followed wherever it can be traced through its transformations, and will be subject when found in its new form to the rights of the original owner or *cestui que trust.* Cook *v.* Tullis, 18 Wall. 341; Neely *v.* Rood, 54 Mich. 134; Pierce *v.* Holzer, 65 Mich. 263. But in all these cases it is held that the fund must be clearly traced into the hands of the person sought to be charged, and that if the trust property does not remain, but has been made way with by the trustee, *cestuis que trustent* have no longer any specific remedy against any part of his estate in his insolvency, but they must come in *pari passu* with the other creditors, and prove against the trustee's estate for the amount due them. This rule has been as steadily adhered to by the courts, both of this country and of England, as any rule which has ever been adopted for the protection of the general creditors of a bankrupt

acted as agents for each other in the collection of checks, notes and drafts, the practice being for each to credit the other for checks when received, and for drafts and notes when advised of their payment. When a check was returned unpaid, after being credited, the amount thereof was charged back again. The amounts thus collected were mingled with the general funds of the bank. The plaintiff bank sent to the bank of which defendant had been appointed receiver, the bank becoming insolvent, a note for "collection and credit," which, on maturity, was paid by a check, and credit was immediately given on the books. The collecting bank failing, the check passed into the hands of the receiver. In this action against the receiver to recover this check

or of an insolvent. It is not seriously contended that the claim of the petitioners comes within the rule stated, but it is insisted that they have the right to the order asked for, under the principle asserted in Carley *v.* Graves, 85 Mich. 483, in which Chief Justice Champlin said, in relation to the trust fund then under consideration, that 'it cannot be specifically traced, but there is enough in the proof to warrant the inference that it has mingled the trust fund with its own individual means, and has rendered it impossible to be specifically traced into other property in its hands, and that it has been used by the company either to pay off its debts or to increase its assets; in either case it would be to the benefit of its estate,' and under those facts he applied the principle laid down by a divided court in McLeod *v.* Evans, 66 Wis. 401; s. c., 28 N. W. Rep. 173, in support of the position, and held that the petitioner was entitled to the order." Commenting upon this expression of law by the chief justice, it was said: "Without discussing the extent to which the language used in that case would seem to imply a departure from, or rather an enlargement of, the general rule first stated, it is sufficient to say that no such condition exists here. There was no appropriation of the proceeds of the check; no mingling of the money realized from it with the assets of the bank for its own benefit, as there was no money realized from it, nor any use made of it by the bank, either to pay off its debts or to increase its assets. For these reasons no possible benefit could accrue to the general creditors of the bank on account of the transaction referred to. To adopt a rule which would permit the petitioners, under the facts of this case, to impose upon this transaction the character of a trust, enforceable as such against the receiver, without either tracing any of its results into his hands, or showing that it was for the benefit of those who have an interest in the assets, thus enabling them, with others similarly situated, to convert to the payment of their own debt the assets of the bank, to the exclusion of the general depositors, whose money, as it is plain to be seen from the record, was the source from which all the assets of the bank were obtained, would be grossly inequitable and would be an unwise departure from those safe rules which the courts have adopted and very generally adhered to in relation to the rights and obligations existing between trustees and *cestuis que trustent.*"

or its proceeds, it was held by a federal court that, in view of the course of dealing, the two banks stood in the relation of debtor and creditor with respect to the amount of the check, and that it became a part of the assets of the insolvent bank.[1] The United States Circuit Court for the northern district of Alabama has held that a bank which collected a draft sent to it by another bank for collection, with directions to remit the proceeds to a third bank for the owner's account, did not thereby become a trustee, so that the fund could be followed into the hands of a receiver, although it had become mixed with the other cash of the bank before his appointment, especially where it appeared that the business was carried on and money paid out for several days after the collection was properly made.[2] In a case where a corporation had sent to a bank for collection a draft on one of its debtors, which he paid by a check on the bank, and the bank remitted in payment a check upon which in the end the corporation failed to realize its money, the bank, by its owner in the meantime, having made an assignment, the corporation procured an order from the court that the assignee of the insolvent banker show cause why its claim should not be declared preferred to that of other creditors. On the hearing the court decided it preferred. Upon appeal to the Supreme Court of Wisconsin, a majority of the court reversed the judgment of the court below, and held that the claim was not a preferred one.[3] A receiver for a bank had been appointed in accordance with the prayer of

[1] Franklin County Nat. Bank *v.* Beal, Receiver, (1892) 49 Fed. Rep. 606. Cf., Marine Bank *v.* Fulton Bank, 2 Wall. 252; Manufacturers' Nat. Bank *v.* Continental Bank, 148 Mass. 555; s. c., 20 N. E. Rep. 193; Levi *v.* Bank, 5 Dill. 104.

[2] Merchants & Farmers' Bank *v.* Austin, (1891) 48 Fed. Rep. 25. See, on this rule, Case *v.* Beauregard, 1 Woods, 126; Union National Bank of Chicago *v.* Goetz, 138 Ill. 127; s. c., 27 N. E. Rep. 907; Peters *v.* Bain, 133 U. S. 693; s. c., 10 Sup. Ct. Rep. 361; McLeod *v.* Evans, 66 Wis. 401; s. c., 28 N. W. Rep. 173; National Bank *v.* Insurance Co., 104 U. S. 54; Bank *v.* Armstrong, 42 Fed. Rep. 193; Bank *v.* Dowd, 38 Fed. Rep. 172; Railroad Co. *v.* Johnston, 133 U. S. 577; s. c., 10 Sup. Ct. Rep. 393.

[3] Nonotuck Silk Co. *v.* Flanders, (Wis. 1894) 58 N. W. Rep. 383. CASSODAY, J., speaking for the majority, said: "If plaintiff [was] entitled to such preference at all it must be by virtue of some established principle of equity or the common law," and proceeded to discuss the question in these words: "'The early English cases only went to the extent of holding, in effect, that the owner of property intrusted to an agent, factor, bailee or other trustee could follow and retake his property from the possession of such trustee, or others in privity with him, and not a *bona fide* purchaser for value, whether such property remained

a bill filed in equity by some of its creditors. A corporation had forwarded to the bank a draft for "collection and returns." The bank had accepted a check of the drawee, one of its depositors, and, without separating the amount from the general mass of its moneys, charged the same to the drawee, and credited the drawer on its books. The corporation which had sent the draft, and been, as above stated, credited with the amount, intervened in the suit, and asked that the receiver be ordered to pay the amount of its claim. The contention of the claimant was that in the collec-

in its original form, or in some different or substituted form, so long as it could be ascertained to be the same property, or the product or proceeds thereof, but that such right ceased when the means of ascertainment failed, or when the subject of the trust was money, or had been converted into money, and then mixed and confounded in a general mass of money of the same description, so as to be no longer divisible or distinguishable. This is apparent from the opinion of Lord Ellenborough, Ch. J., written nearly 80 years ago, reviewing the adjudications prior to that date. Taylor *v.* Plumer, 3 Maule & S. 575. But the more recent rule in England as to following trust moneys is broader, and goes to the extent of holding, in effect, that 'if money held by a person in a fiduciary character, though not as trustee, has been paid by him to his account at his bankers, the person for whom he held the money can follow it and has a charge on the balance in the banker's hands;' that 'if a person who holds money as a trustee, or in a fiduciary character, pays it to his account at his banker's, and mixes it with his own money, and afterwards draws out sums by checks in the ordinary manner, * * * the drawer must be taken to have drawn out his own money in preference to the trust money.' In re Hallett's Estate (Knatchbull *v.* Hallett), 13 Ch. Div. 696, overruling some former English cases. 'In that case there was no dispute but what the money received by the trustee for the property wrongfully converted was deposited with his bankers to the credit of his account, and that the same remained at his bankers' mixed with his own money at the time of his death.' But in the leading opinion by Jessel, M. R., in that case, and by way of quoting Mr. Justice Fry approvingly, it is said: 'The guiding principle is that a trustee cannot assert a title of his own to trust property. If he destroys a trust fund by dissipating it altogether, there remains nothing to be the subject of the trust. But so long as the trust property can be traced and followed into other property into which it has been converted, that remains subject to the trust. Ibid. p. 719.' That case is as favorable to the claim of the plaintiff as any in the English courts, and yet it nowhere questions the proposition that the owner of the property or money intrusted is entitled to a preference over other creditors of an insolvent estate out of property or assets to which no part of the trust fund, or the proceeds thereof, is traceable. All such cases turn upon the question of fact whether the trust property or fund, or the proceeds thereof, are traceable into any specific property or fund. Ex parte Hardcastle (In re Mawson), 44 Law T. 524. Thus, in Re Cavin *v.* Gleason, 105 N. Y. 256; s. c., 11 N. E. Rep. 504, it was held that, to entitle the trust creditor to such a preference, it must, at least, be made to

tion of its draft on its debtor the insolvent bank had acted as its agent and trustee, and that it was entitled, as against the other creditors of the bank, to priority of payment out of the bank's assets; that, notwithstanding the money collected from its debtor was intermingled with the general assets of the bank, and could not be identified or specifically traced into the hands of the receiver, yet a court of equity would subtract the amount due claimant from the funds in the hands of the receiver, and would

appear that the fund or property of the insolvent, remaining for distribution, includes proceeds of the trust estate." To the same effect, Atkinson *v.* Printing Co., 114 N. Y. 168; s. c., 21 N. E. Rep. 178; Holmes *v.* Gilman, 138 N. Y. 376; s. c., 34 N. E. Rep. 205. In Little *v.* Chadwick, 151 Mass. 110; s. c., 23 N. E. Rep. 1005, the court said: "When trust money becomes so mixed up with the trustee's individual funds that it is impossible to trace and identify it as entering into some specific property, the trust ceases. The court will go as far as it can in thus tracing and following trust money; but when, as a matter of fact, it cannot be traced, the equitable right of the *cestui que trust* to follow it fails." The Michigan court cited as to the same effect as the Massachusetts and other cases above referred to: Goodell *v.* Buck, 67 Me. 514; Steamboat Co. *v.* Locke, 73 Me. 370; Englar *v.* Offutt, 70 Md. 78; s. c., 16 Atl. Rep. 497; Thompson's Appeal, 22 Pa. St. 16; Columbian Bank's Estate, 147 Pa. St. 440; s. c., 23 Atl. Rep. 625, 626, 628; Appeal of Hopkins, (Pa.) 9 Atl. Rep. 867; Bank *v.* Goetz, 138 Ill. 127; s. c., 27 N. E. Rep. 907; Neely *v.* Rood, 54 Mich. 134; s. c., 19 N. W. Rep. 920; Sherwood *v.* Bank, 94 Mich. 78; s. c., 53 N. W. Rep. 923; Elevator Co. *v.* Clark, (N. D.) 53 N. W. Rep. 175; National Bank *v.* Insurance Co., 104 U. S. 54, 68; Peters *v.* Bain, 133 U. S. 670, 693; s. c., 10 Sup. Ct. Rep. 354; 2 Story Eq. Jur. §§ 1258, 1259; 2 Pom. Eq. Jur. § 1058; 1 Lewin Trusts (1st Am. ed.), 241. "In speaking of following trust moneys into other property, it is stated in one of the New York cases cited that 'the right has its basis in the right of property.' It never was based upon the theory of preference by reason of an unlawful conversion. This is made clear by a recent and well-considered opinion by the Supreme Court of Rhode Island. Slater v. Oriental Mills, (R. I.) 27 Atl. Rep. 443. It follows that the mere fact that [the insolvent's] bank used the plaintiff's money towards paying its indebtedness, before making the assignment, did not authorize a preference to the plaintiff over [the assignor's] other creditors, out of his other property and assets. This is made plain by an illustration having judicial sanction in the case last cited: 'Suppose that an insolvent debtor, D., has only $1,000 of property, but is indebted to the amount of $2,000, one-half of which is due to A., and the other half to B. In this condition of things, D.'s property can only pay fifty per cent of his debts. By such distribution A. and B. would each be equitably entitled to $500. Now, suppose D., while in that condition, collects $1,000 for F., but, instead of remitting the money, as he should, he uses it in paying his debt in full to A. By so doing D. has not increased his assets a penny, nor decreased his aggregate indebtedness a penny. The only difference is that he now owes

compel him to restore it to the claimant, because the amount had been collected by the bank as its agent and trustee, and had increased *pro tanto* its general assets. The United States Circuit Court of Appeals for the fifth circuit held that the money was held by the insolvent bank as the agent of the claimant, and not as trustee; and that after the bank became insolvent the claimant was a mere general creditor, and not entitled to priority of payment out of the bank's assets.[1] The Constitution of the state of Alabama provides that "depositors who have not stipulated for interest shall for such deposits be entitled, in case of insolvency,

$1,000 each to B. and F., whereas he previously owed $1,000 each to A. and B. Now if F. is to have preference over B. then his claim will absorb the entire amount of D.'s property, leaving nothing whatever for B. In other words, the $500 to which B. was equitably entitled from his insolvent debtor, upon a fair distribution of the estate, has, without any fault of his, been paid to another, merely in consequence of the wrongful act of the debtor.' Ibid. and dissenting opinion in Francis *v.* Evans, 69 Wis. 115, 123. See, also, McClure *v.* Board, (Col.) 34 Pac. Rep. 763. We must hold that the plaintiff has no rights to a preference over [the banker's] other creditors in the distribution of his estate in the hands of the defendant, as assignee, and into which no part of the plaintiff's money has been issued." The majority of the court said that "in so far as McLeod *v.* Evans, 66 Wis. 401; s. c., 28 N. W. Rep. 173, 214; Francis *v.* Evans, 69 Wis. 115; s. c., 33 N. W. Rep. 93; and Bowers *v.* Evans, 71 Wis. 133; s. c., 36 N. W. Rep. 629, are in conflict with the rules above indicated, they must be regarded as overruled." These cases, ORTON, Ch. J., dissenting, said, ruled this case.

[1] Anheuser-Busch Brewing Assn. *v.* Clayton, (1893) 56 Fed. Rep. 759. TOULMIN, D. J., in the opinion delivered, said: "The relation between [the claimant] and [the insolvent bank] as to the draft on [its debtor] sent by the former to the latter for collection was that of principal and agent; but, in order to enforce a trust in favor of [the claimant] as to any money collected on said draft, it must be specifically traceable into the hands of the receiver. Commercial Nat. Bank *v.* Armstrong, 39 Fed. Rep. 684; same case in Supreme Court of the United States, 148 U. S. 50; 13 Sup. Ct. Rep. 533. Accepting [the drawer's] check in payment of his debt to [the claimant], and charging the amount of it on [the drawer's] account by the bank, was but a shifting of its liability, whereby it became [the claimant's] debtor and assumed the obligation to pay it the amount of the check less exchange. There is nothing to indicate that this amount was separated and kept unmingled with the bank's own money; but, on the contrary, it is conceded that it is undistinguishable from the mass of the bank's own money and cannot be turned to and identified in the hands of the receiver. This being so [the claimant] has no better equity than the other creditors of the bank, and is entitled to no priority over them." See, in line with the text, Maury *v.* Mason, 8 Port. (Ala.) 236; Goldsmith *v.* Stetson, 30 Ala. 164; Parker *v.* Jones, 67 Ala. 236: Illinois Trust & Savings Bank *v.* First Nat. Bank, 15 Fed. Rep. 858; Bank *v.* Dowd, 38 Fed. Rep. 172; Bank *v.* Rus-

to preference of payment over all other creditors." Another contention of claimant in this case was that under this provision of the Constitution of Alabama it at least had a right to be classed among depositors who had not stipulated for interest on deposits, and, therefore, entitled as among that class to be preferred to the other creditors. The Court of Appeals held adversely to this contention.[1] These facts appeared in a case before the Supreme Court of Minnesota: A firm deposited with a bank a check for collection. The bank sent it to the clearing house, where it was used in balancing the account of the bank. Afterwards, on the same day, the bank made an assignment for the benefit of its creditors, but neither the check nor the direct proceeds of the check came to the assignee. In the proceedings in insolvency the lower court, upon an application of the firm depositing the check with the bank, ordered the assignee of the bank to pay to the firm the amount called for by the check. The Supreme Court reversed this order, holding that the depositors

sell, 2 Dill. 215; First Nat. Bank *v.* Armstrong, 42 Fed. Rep. 193.

[1] Anheuser-Busch Brewing Assn. *v.* Clayton, (1893) 56 Fed. Rep. 759. TOULMIN, D. J., said upon this contention: "A bank depositor is one who delivers to or leaves with a bank money subject to his order. And. Law Dict. 343, 344; Newmark Bank Deposits, § 12. Deposits made with bankers are either general or special. In the case of a special deposit of money the bank merely assumes the charge or control of it, without authority to use it, and the depositor is entitled to receive back the identical money deposited. 1 Morse Banks, § 183. The relation thus created is that of bailor and bailee. Money received by a bank on general deposit becomes the property of the bank and can be used by it as other moneys belonging to it, the relation between the bank and the depositor being that of debtor and creditor: 'that kind of deposit of money peculiar to banking business, in which the depositor, for his own convenience, parts with the title to his money and loans it to the banker.' Commercial Nat. Bank *v.* Armstrong, 39 Fed. Rep. 684; Wray *v.* Insurance Co., 34 Ala. 58; Alston *v.* State, 92 Ala. 124; s. c., 9 So. Rep. 732. The contention of the learned counsel for [the claimant] is that his case meets this definition of a general depositor. We cannot agree with this contention. [Claimant] did not leave [its] money with [the insolvent bank] subject to its order or to be returned to it on call. It did not for its own convenience part with the title to its money and loan it to the bank. There was no contract, express or implied, that the collection from [its debtor] on [claimant's] account was to be a deposit of any kind, but it is clear that it was intended that the money received from [the debtor] should be remitted in 'a reasonable time' from date of collection. [Claimant] inclosed its draft on [the debtor] to the [bank] for 'collection and returns.' [The debtor] took up the draft with his check on [the bank], and on the same day the latter forwarded to [claimant] exchange on a New York bank for the amount of [the debtor's]

of the check were not entitled to any preference over other claims against the insolvent.[1] A national bank having been notified by the comptroller that its capital was impaired, it was agreed that it might continue business on the directors putting in $100,000 in cash, and retiring that amount of objectionable securities. The directors contributed the sum required in cash, an account being opened with trustees appointed by the directors to manage the fund, with full power, as far as the bank was concerned, and to account therefor to the contributors in such manner as to protect the equities of each individual and the bank, in relation to the bank and its legal rights. It was understood between the trustees and the bank examiner that the securities to be retired were to be designated by the comptroller or examiner, but there was no such understanding with the comptroller. The full amount of objectionable securities had not been selected and given to the trustees when the bank was closed, the receiver taking and proceeding to collect the whole assets. It was claimed by the trustees for the directors that the balance was held by the bank as a special or trust fund; that it did not form part of the assets of the bank; that the receiver was chargeable with notice of the nature of the fund; and that when the receiver was placed in control of the bank this balance came into his hands impressed with the trust originally pertaining thereto; and that he must account therefor for the use of the directors. SHIRAS, J., of the United States Circuit Court, held, however, that the receiver was not required to account for the balance of the $100,000 as a special trust fund, but merely as a debt.[2]

indebtedness. The draft was not paid, but this did not alter the relation between [the claimant] and [the bank]. The bank still owes the debt."

[1] In re Seven Corners' Bank, (Minn. 1894) 59 N. W. Rep. 633, GILFILLAN, Ch. J., said: "The case is not essentially different from what it would have been had the bank received the money on the check from the bank on which it was drawn and paid with it checks drawn on itself or used it in any other way in its business. * * * Had the check come to the hands of the assignee an order to deliver it to [the depositors] would have been proper. In such case the specific property would have been that of [the depositors]. As it was, there existed nothing but a cause of action against he bank for conversion of the check or of the money, its proceeds; and, as such, it stands on the same footing as any other claim upon the assigned assets based on a conversion of money or other property. To allow such claims to be paid in full out of the assets, when all claims cannot be paid in full, would give a preference to such claims. There is nothing in the insolvent law justifying it."

[2] Booth *v.* Welles, (1890) 42 Fed. Rep. 11.

CHAPTER XIV.

LIABILITY OF BANK SHAREHOLDERS.

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§ 358. **Rules generally.**— The stockholders of a banking corporation are primary debtors to the depositors, and are co-ordinately responsible with the bank. Its liability and that of the stockholders commences at the same time.[1] A subscriber for shares of the stock of a bank will be held responsible as a stockholder, though he may not have paid for his stock or received certificates therefor.[2] Persons who hold stock in pledge, the certificates of which stand on the books of the bank in the name of the pledgee, are, in contemplation of the National Banking Act, stockholders, and so long as they thus hold the stock in pledge are responsible to the creditors of the bank in proportion to the amount so held.[3] Subscription to the stock of a national bank, and payment in full with entry of name on its books as a stockholder, makes the subscriber a stockholder without taking out a certificate.[4] The responsibility of a stockholder in a national bank for further assessments on the stock will cease on his selling to the bank, as agent for an unknown principal, his stock, and

[1] Mitchell *v.* Beckman, (1883) 64 Cal. 117; citing Mokelumne Hill Canal & Mining Co. *v.* Woodbury, 14 Cal. 265.

[2] Mitchell *v.* Beckman, (1883) 64 Cal. 117; citing Chaffin *v.* Cummings, 37 Me. 83; Spear *v.* Crawford, 14 Wend. 20; Chester Glass Co. *v.* Dewey, 16 Mass. 94; In re South Mountain Consolidated Mining Co., 7 Sawy. 30.

[3] Magruder, etc., *v.* Colston, 44 Md. 349.

[4] Pacific National Bank *v.* Eaton, 141 U. S. 227; Thayer *v.* Butler, 141 U. S. 234; Butler *v.* Eaton, 141 U. S. 240.

delivering to the bank his certificate and power of attorney for transfer, in blank, though no formal transfer be made.[1] Where shares of stock in a national bank have been hypothecated, and placed in the hands of the transferee, the transferee will be subjected to all the liabilities of ordinary owners of shares. It is for the reason that the property is in his name and the legal ownership appears to be in him.[2] One who is chargeable as a shareholder in a national bank will not be relieved from his liability by failure on the part of an officer of the bank to comply with the provisions of the act as to these banking associations requiring a list of the stockholders to be kept, accessible to all persons, by reason of which he is not shown to be a shareholder.[3] In an action based upon an assessment made by the comptroller of the currency on the stockholders of a national bank the Supreme Court of the United States held that a transfer of stock in a bank to a person without his or her knowledge or consent did not of itself impose upon the transferee the liability attached by law to the position of a stockholder in the association; but if, after the transfer, the transferee approved or acquiesced in it, or in any way ratified it (as, for instance, by joining in an application to convert the bank, which was originally a savings bank in the District of Columbia, into a national bank), or accepted any benefit arising from the ownership of such stock, he or she became liable to be treated as a stockholder with such responsibility as the law imposed in the case of shareholders of a national banking association; and this liability would be the same whether new certificates had or had not been issued to the transferee after the transfer. And the indorsement by the payee of a check which appeared on its face to be drawn by the cashier of the bank in payment of a dividend due the payee as a stockholder, was held to estop the payee from

[1] Whitbeck *v.* Mercantile Bank, 127 U. S. 193.

[2] Wheelock *v.* Kost, (1875) 77 Ill. 296; citing Morse on Banking, 432; Adderly *v.* Storm, 6 Hill, 624; In re Empire City Bank, 18 N. Y. 199. The facts in Wheelock *v.* Kost, *supra*, were that the defendant made a loan to the bank, and made his promissory note partly as an accommodation to the bank, to be held among their other assets, and fifty shares of its stock, equal in value to $5,000, were issued to him, as security for his loans, and as indemnity against liability on his note. The court held him liable to the creditors of the bank as a stockholder. As to the liability of shareholders of a national bank to the creditors of the bank, see Laing *v.* Burley, 101 Ill. 591. As to stockholder's liability on obligations to a bank, see Finnell *v.* Sandford, (1856) 17 B. Mon. (Ky.) 758.

[3] Hale *v.* Walker, 31 Iowa, 344.

denying knowledge of its contents or ownership of the shares.[1] It has been held in a federal court that one who subscribed and paid for a specified number of shares of a "proposed increase" of the capital stock of a national bank, which increase, in fact, was never issued, and to whom the bank officials transferred, instead, old stock of the bank without his knowledge or consent, was not a "shareholder" within the meaning of that section of the Revised Statutes of the United States, which imposes individual liability on the shareholders for the debts of national banks. And the fact that such a subscriber for the new shares received a dividend on the old shares so transferred to him, did not estop him from denying his liability as a shareholder where such dividend was received in the belief that it was paid to him by virtue of his subscription to the proposed new stock.[2] It appeared in a case before the United States Supreme Court that some of the creditors of this bank, after it determined to go into voluntary liquidation, made settlements of their claims for some cash and certain papers belonging to the bank, indorsed and guaranteed by the president in the name of the bank. They afterwards reduced these claims, growing out of the indorsement or guaranty by the president, to judgment, and in the form of judgments against the bank presented them, and they were allowed a *pro rata* for the sums realized in this action of creditors against stockholders with the other creditors in the decree made. The Supreme Court held that this was erroneous.[3]

[1] Keyser *v.* Hitz, (1890) 133 U. S. 138; s. c., 10 Sup. Ct. Rep. 290.

[2] Stephens *v.* Follett, (1890) 43 Fed. Rep. 842.

[3] Richmond *v.* Irons, (1887) 121 U. S. 27. Mr. Justice MATTHEWS, for the court, said: "Those creditors who made settlements after the bank was put in liquidation, and received from the president in that settlement paper of the bank, or, as in some cases, the individual notes of [the president] himself, indorsed or guaranteed in the name of the bank, are not to be considered as creditors of the bank, entitled to subject the stockholders to individual liability. The individual liability of the stockholders, as imposed by and expressed in the statute, is, indeed, for all the contracts, debts and engagements of such association, but that must be restricted in its meaning to such contracts, debts and engagements as have been duly contracted in the ordinary course of its business. That business ceased when the bank went into liquidation; after that there was no authority on the part of the officers of the bank to transact any business in the name of the bank so as to bind its shareholders, except that which is implied in the duty of liquidation, unless such authority had been expressly conferred by the shareholders. No such express authority appears in this case, and the power of

§ 359. Rule under Minnesota statute.— One acquiring stock in a banking corporation incurs the statutory liability, not only in respect to corporate debts contracted after he became a stockholder, but also in respect to debts contracted before that time.[1]

the president or other officer of the bank to bind it by transactions after it was put into liquidation is that which results by implication from the duty to wind up and close its affairs. That duty consists in the collection and reduction to money of the assets of the bank, and the payment of creditors equally and ratably, so far as the assets prove sufficient. Payments, of course, may be made in the bills receivable and other assets of the bank in *specie*, and the title to such paper may be transferred by the president or cashier by an indorsement suitable to the purpose in the name of the bank, but such indorsement and use of the name of the bank is in liquidation, and merely for the purpose of transferring title. It can have no other effect as against the shareholders by creating a new obligation. It does not constitute a liability, contract or engagement of the bank for which they can be held to be individually responsible. Every creditor of the bank, receiving its assets under such circumstances, knows the fact of liquidation, and is chargeable with knowledge of its consequences; he takes the assets received at his own peril; he is dealing with officers of the bank only for the purpose of winding up its affairs. If he accepts something in lieu of the existing obligations looking to future payment, it must be from other parties. It is not within the power of the officers of the bank, without express authority, by such means to prolong indefinitely an obligation on the part of the shareholders, which is imposed by the statute only as a means of securing the payment of debts of an insolvent bank when it is no longer able to continue business, and for the purpose of effectually winding up its affairs. This is the very meaning of the word 'liquidation.'" Mr. Justice STORY said, in Fleckner *v.* Bank of the United States, 8 Wheat. 338, 362: "Its ordinary sense, as given by lexicographers, is to clear away, to lessen debt, and in common parlance, especially among merchants, to liquidate the balance is to pay it." In White *v.* Knox, 111 U. S. 784, 787, it was said: "The business of the bank must stop when insolvency is declared." In National Bank *v.* Insurance Co., 104 U. S. 54, the liquidation of such an association was said to be like that which follows the dissolution of a copartnership.

[1] Olson *v.* State Bank, (Minn. 1894) 59 N. W. Rep. 635. Discussing the question GILFILLAN, Ch. J., said: "The decisions of the courts in the different states seem at variance, the greater number holding that those who own the stocks when the remedy is sought by the creditors — that is, when the action to enforce the liability is brought — are liable in respect to all the corporate debts, no matter whether contracted before or after they acquired their stock. The decisions in each state are based on the terms of the statute in each, as construed by the court; and, as the terms of the statutes in the different states vary, but little aid is afforded by the decisions in other states. Our statute is Gen. St. 1878, chap. 33, § 14: 'Every person becoming a stockholder therein, shall, in proportion to his interest, succeed to all the rights and be subject to all the liabilities of prior stockholders.' Section 2: 'And the stockholders in each

§ 360. **Rules under Michigan statute.**—In an action by the receiver of an insolvent bank to enforce the liability of a stockholder under the provisions of the Banking Act of the state of Michigan, declaring that "the stockl olders of every bank shall be individually liable, equally and ratably, and not one for another, for the benefit of the depositors in said bank to the amount of their stock at the par value thereof, in addition to the said stock, * * *" it appeared by the record that, about the time the bank was organized, the defendant negotiated with one who became cashier of the bank for the purchase of stock. It appeared from the stock ledger that under a certain date there was issued to defendant a certificate of stock, the stock ledger stating that the stock was transferred from a subscription of another. It further appeared that a certificate was, in fact, issued to the defendant, and that he received dividends for several years. It was claimed for the defendant that he was not a stockholder, and urged further that, not being an original subscriber to the capital stock, the only way in which he could become a stockholder was by securing a transfer of some of the stock subscribed for by others, and that no formal transfer appeared upon the bank books, and, hence, that he never legally became a stockholder.

bank shall be individually liable in an amount equal to double the amount of stock owned by them for all the debts of such bank, and such individual liability shall continue for one year after any transfer or sale of stock by any stockholder or stockholders.' The terms 'all the debts of such bank' are general, unqualified, and include all debts, without regard to when incurred. To exclude from their meaning those incurred prior to becoming a stockholder we would have to add after the word 'bank' some such words as 'contracted after they acquired the stock,' and to hold that the legislature, while intending what such words would mean, omitted, for some reason or other, to express such meaning by apt terms. But the point was really decided in this state thirty years ago, and the decision has been acquiesced in, accepted and regarded as the law ever since, till questioned in this case. In Gebhard *v.* Eastman, 7 Minn. 56, the court construes a statute somewhat less emphatic in its terms than section 21, chapter 33. The terms in that case were, 'Each of the stockholders of said company shall be personally liable for the debts of said company to an amount equal to the amount of capital stock held by such stockholder, and no more.' It was held that the act created a personal liability against each stockholder at the time that the debt was contracted, 'and all that may voluntarily become so at any subsequent period prior to satisfaction.' Noting that this statute does what that did not, to wit, limit the liability to one year after the stockholder shall have transferred his stock, that decision disposes of the question here in hand."

The Supreme Court of Michigan held adversely to this contention.[1] The court also held adversely to the other contention on the part of the defendant, that, if he ever legally assumed the relation of stockholder, he was induced to enter into the contract by fraud.[2]

[1] Bissell, Receiver, *v.* Heath, (1894) 98 Mich. 472. The court said: "The answer to this [contention] is that the evidence of the transfer was sufficient to satisfy the corporators. The stock was, in fact, issued, and the books of the company showed it sufficiently. Grand Rapids Savings Bank *v.* Warren, 52 Mich. 557. The corporation was bound by the issue of the stock. It could waive the formality of any assignment by [the original subscriber to the stock], and, having done so, could not thereafter deny defendant's rights on the ground that he had failed to produce evidence of an assignment from an original subscriber to the capital stock." Citing Mor. Priv. Corp. § 844.

[2] Bissell, Receiver, *v.* Heath, (1894) 98 Mich. 472. It was said by the court that it was "conceded by [defendant's] counsel that there are authorities which maintain that it is not open to a stockholder, when the rights of creditors have intervened, to assert the claim that he was induced by fraud to become a stockholder; but it is insisted that the true rule is that asserted by Lord CAIRNS in Smith's Case, 2 Ch. App. 604, that it is one of the risks which creditors are liable to that it may turn out that some person whose name appears as stockholder on the list has a right to have his name taken from the list. In the case cited, however," said the court, "the action was taken before any steps had been taken to wind up the affairs of the corporation under the Winding Up Act." They then proceeded to discuss the questions involved, as follows: "In Stone *v.* Bank, 3 C. P. Div. 282, it was held that where the corporation has gone into liquidation, and is proceeding under the Winding Up Act, to make calls to satisfy claims of creditors, it is too late for one who has, up to that time, allowed his name to appear as a stockholder, to avoid liability on the ground that his subscription was obtained by fraud. The question was touched upon by this court in Duffield *v.* Wire & Iron Works, 64 Mich. 293. In that case plaintiff had been induced to become a stockholder by fraud, and, on discovery of the fraud, tendered back the shares and dividends received, and brought an action against the corporation before any assignment was made for the benefit of creditors. On the question of the plaintiff's right to recover, under the circumstances, the court was evenly divided, Justices CHAMPLIN and MORSE, being of the opinion that the plaintiff could not rescind the contract after the rights of creditors had intervened, even though no steps had actually been taken to wind up the affairs of the corporation. Chief Justice CAMPBELL and Mr. Justice SHERWOOD were of the opposite opinion. We do not deem it necessary to decide which of the two opinions we would follow in a case presenting the same state of facts, as we think that, even under the doctrine of Justice CAMPBELL's opinion, the defendant in this case cannot be relieved. Justice CAMPBELL lays stress upon the fact that, under the statute relating to manufacturing corporations, the stockholders are not personally liable to contribute beyond what will pay up for their stock, and that creditors cannot enforce any rights against fully-

§ 361. Stockholder relieved from liability by a sale of his stock through a broker.— In an action brought by the receiver of a national bank to charge defendant as a stockholder, it appeared that the latter, in good faith, and without intent to evade his responsibility as a stockholder, the owner of a number of its shares, sold them to a broker, to whom he delivered his stock certificate, and a power to transfer them, leaving blanks for the names of the attorney and transferee. The broker sold them to the president of the bank, who gave his individual check in payment therefor, and received the certificate and power. By the directions of the president, a bookkeeper of the bank inserted his own name as attorney, and transferred the stock to the president of the bank as "trustee" on the official stock register. The entries in the stock ledger and other books of the bank showed that the president purchased the stock for the bank, and reimbursed himself with its funds. The bookkeeper had actual knowledge of all the facts. The argument of the receiver, before the Supreme Court of the United States, to support his action, praying that the purchase on the part of the bank be set aside, and that the defendant be compelled to repay the money received to him and the president of the bank to re-transfer to him the shares on the books of the bank, was substantially that the transfer of the stock was not complete until made on the books of the bank, and the attorney who made it knew that the purchase was by the bank and with its funds, and his knowledge was the knowledge of defendant. The court held that as the bookkeeper was the agent of the bank, his knowledge of the transaction could not be imputed to the defendant, and that the suit could not be maintained.[1]

paid stock. But such is not the case with corporations organized under the Banking Law. It is apparent that Justice CAMPBELL recognized the doctrine of Stone *v.* Bank, *supra.* We think that the defendant in this case cannot, after having permitted the depositors of the bank to rely upon his apparent ownership of this stock, and after having received dividends upon the stock for years, which he has not tendered back, be heard now to repudiate his liability." Citing Mor. Priv. Corp. § 840; Chubb *v.* Upton, 95 U. S. 665; Cook Stock & S. §§ 163, 164.

[1] Johnson *v.* Laflin, (1880) 103 U. S. 800. *Arguendo,* Mr. Justice FIELD, in the opinion, said: "The general doctrine that the principal in a transaction is chargeable with notice of matters affecting its validity, coming to the knowledge of his agent pending the proceeding, is not questioned. Had * * * the bookkeeper been appointed by [defendant] to make the

§ 362. **Pledgee of stock incurs no liability.**—In a case before the Supreme Court of the United States it was held that a pledgee of shares of stock in a national bank, who, in good faith and with no fraudulent intent, takes the security for his benefit in the name of an irresponsible trustee for the avowed purpose

sale, and had he, in negotiating it, learned the facts as to the purchase and use of the funds of the bank, there would be ground to invoke the application of the doctrine. But such was not the position of [the bookkeeper] to [defendant]. The sale was consummated, so far as [defendant] was concerned, when he delivered the certificate, with the power to transfer it to the broker. The latter did not mention the name of the principal for whom he was acting. He declined to give it. [Defendant] had a right, therefore, to treat him as the principal, and if he was competent to make the purchase the sale was valid." As to the transfer of such shares, generally, it was then said: "Shares in the capital stock of associations, under the National Banking Law, are salable and transferable at the will of the owner. They are, in that respect, like other personal property. The statute recognizes this transferability, although it authorizes every association to prescribe the manner of their transfer. Its power in that respect, however, can only go to the extent of prescribing conditions essential to the protection of the association against fraudulent transfers, or such as may be designed to evade the just responsibility of the stockholder. It is to be exercised reasonably. Under the pretense of prescribing the manner of the transfer, the association cannot clog the transfer with useless restrictions, or make it dependent upon the consent of the directors or their stockholders. * * * As between [defendant] and the broker, the transaction was consummated when the certificate was delivered to the latter with the blank power of attorney indorsed, and the money was received from him. As between them the title to the shares then passed; whether that be deemed a legal or equitable one matters not; the right to the shares then vested in the purchaser. The entry of the transaction on the books of the bank, where stock is sold, is required, not for the translation of the title, but for the protection of the parties and others dealing with the bank, and to enable it to know who are its stockholders entitled to vote at their meetings and receive dividends when declared. It is necessary to protect the seller against subsequent liability as a stockholder, and perhaps also to protect the purchaser against proceedings of the seller's creditors. Purchasers and creditors, in the absence of other knowledge, are only bound to look to the books of registry of the bank. But, as between the parties to a sale, it is enough that the certificate is delivered with authority to the purchaser, or any one he may name, to transfer it on the books of the company and the price is paid. If a subsequent transfer of the certificate be refused by the bank, it can be compelled at the instance of either of them. Bank *v.* Lanier, 11 Wall. 369; Webster *v.* Upton, 91 U. S. 65; Bank of Utica *v.* Smalley, 2 Cow. 770; Gilbert *v.* Manchester Iron Co., 11 Wend. 627; Commercial Bank of Buffalo *v.* Kortright, 22 Wend. 348; Sargeant *v.* Franklin Insurance Co., 8 Pick. 90. The transferability of shares in the national banks is not governed by different rules from those which are ordinarily applied to the transfer of shares in other corporate

of avoiding individual liability as a shareholder, and who exercises none of the powers or rights of a stockholder, incurs no liability as such to creditors of the bank in case of its failure.[1] A corporation which holds shares of stock in a national bank as collateral security for a loan, and is carried on the registry of the

bodies. The power of attorney indorsed in the certificate is usually written or printed, with a space in blank for the name of the attorney to be inserted for the accommodation of the purchaser. The subsequent filling up of the blank by him with another name instead of his own, as it may suit his convenience, does not so connect the vendor with the party named as to charge him with the latter's knowledge and thus affect the previous transaction. * * *" The court did not consider that the further position of the receiver in this action, that the assets of the bank constituted a trust fund for the benefit of its creditors, and, where wrongfully diverted, could be followed in whosesoever hands they could be traced, had application to this case. It was said: "Here no assets of the bank were received by [defendant]. What he received came from the broker, the only person with whom he dealt or whom he knew as principal in the negotiation. The circumstance that the purchase was actually in the interest of the bank — though of that fact the broker was ignorant — cannot affect the latter's character as principal, so far as [defendant] was concerned, which he bore in the negotiation. The whole transaction on the part of [defendant] was free from any imputation of fraud. He sold his shares to a person competent to purchase and hold them and received the stipulated price. It would be a perversion of justice and of the ordinary rules governing men in commercial transactions to hold the sale, under such circumstances, vitiated by the relations of the purchaser to others, of which the seller had no knowledge, or any grounds to entertain a suspicion. The validity of the sale of stock cannot be made to depend upon the accident of the immediate purchaser, or of the party to whom he may transfer the certificate, in filling up the blank in the power of attorney with the name of a person to make the formal transfer, who is acquainted with the secret interest of others in the shares purchased. The validity of a sale and its completeness must be determined by the relation which the contracting parties at the time openly bear to each other."

[1] Anderson *v.* Philadelphia Warehouse Company, (1884) 111 U. S. 479, MILLER and MATTHEWS, JJ., dissenting. WAITE, Ch. J., in his opinion for the majority of the court, said: "It is well settled that one who allows himself to appear on the books of a national bank as an owner of its stock is liable to creditors as a shareholder, whether he be the absolute owner or a pledgee only, and that if a registered owner, acting in bad faith, transfers his stock in a failing bank to an irresponsible person for the purpose of escaping liability, or if his transfer is colorable only, the transaction is void as to creditors. National Bank *v.* Case, 99 U S. 628; Bowden *v.* Johnson, 107 U. S. 251. It is also undoubtedly true that the beneficial owner of stock registered in the name of an irresponsible person may, under some circumstances, be liable to creditors as the real shareholder, but it has never, to my knowledge, been held that a mere pledgee of stock is chargeable, where he is not registered as owner." In the conclusion of the opinion it was said: "The security of

bank as the holder of such stock "as pledgee," is not subject, on the bank's insolvency, to the statutory liability of a stockholder.[1] One who is entered on the books of a national bank as the owner of stock, but who is admitted to hold the stock for the true owner, is not liable as a stockholder for the debts of the bank, when the true owner has been adjudged so liable, though nothing may be realized upon the execution of the judgment against the true owner.[2]

the warehouse company was perfected without imposing on the company a shareholder's liability. All this was done in good faith when the bank was in good credit and paying large dividends, and years before its failure, or even its embarrassment. So far as the company was concerned the transfer [to one of its employees] was not made to escape an impending calamity, but to avoid incurring a liability it was unwilling to assume, and which it was at perfect liberty to shun." In the dissenting opinion, rendered by MILLER, J., it was said: "I think if in any case between private persons one of them had placed property in the hands of minors, servants, or other irresponsible persons, for the purpose of escaping the responsibility attaching to the ownership of such property, while securing all the advantages of such ownership, it would be held to be a transaction which could not be supported on any legal or equitable principle. It does not remove this case from the control of that principle that the parties to be injured are the unknown creditors of the bank, who are, by this means, deprived of the right which they have to resort to a responsible shareholder for the contribution which the law gives for their benefit. If not an actual fraud, it is a fraud upon the Banking Law, and was so intended to be by both the original holders of the bank shares and the officers of the warehouse company, by which the latter could control the shares without the responsibility which the law attaches to the owner."

[1] Pauly *v.* State Loan & Trust Co., (1893) 56 Fed. Rep. 430. It was said by the court: "The precise question involved was not presented in any of the numerous cases cited by counsel. But, in my opinion, the doctrine of the case of Anderson *v.* Warehouse Co., 111 U. S. 479; s. c., 4 Sup. Ct. Rep. 525, carried to its logical conclusion, exempts the defendant from the liability with which it is sought to be charged. In that case the Supreme Court, while declaring it to be well settled that one who allows himself to appear on the books of a national bank as an owner of its stock is liable to the creditors as a shareholder, whether he be the absolute owner or pledgee only, and that if a registered owner, acting in bad faith, transfers his stock in a failing bank to an irresponsible person, for the purpose of escaping liability, or if his transfer is colorable only, the transaction is void as to creditors, and that it is also true that the beneficial owner of stock registered in the name of an irresponsible person may, under some circumstances, be liable to creditors as the real shareholder, said it knew of no case that held that a mere pledgee of stock is chargeable where he is not registered as owner."

[2] Yardley *v.* Wilgus, (1893) 56 Fed. Rep. 965.

§ 363. **When a stockholder is relieved from liability.**— It appeared in an action by a receiver of a national bank to enforce an assessment under the Revised Statutes of the United States, section 5151, against a person credited on the transfer books as a stockholder, that nearly a year before the failure of the bank he had sold this stock to a broker for an indisclosed principal; that he indorsed the same, and requested the broker to inform the cashier of the transaction, and to have the stock transferred; that the broker accordingly handed the stock to the cashier, gave him the necessary information, and requested him to make the transfer. This the cashier promised to do, but, in fact, the transfer was never made. The certificate recited that it was transferable on the books of the company "by indorsement hereon and surrender of this certificate." It was held by the United States Circuit Court for the northern district of California that, in requesting the cashier to make the transfer, the broker acted as the seller's agent, and that the latter did all that was required of him as a prudent business man, and could not be held liable as a stockholder.[1]

§ 364. **The rule where shares are transferred to avoid liability.**— In an action by a receiver of an insolvent national bank against the transferrer and transferee of shares where the testimony showed to the minds of the Supreme Court of the United States that there was an attempt on the part of a holder of shares of stock in a national bank to escape personal liability as a shareholder by collusion with and transfer of the shares to one not solvent and responsible, the court, after reciting the section of Revised Statutes applicable to the matter, thus declared the law governing in such case: "As [a] shareholder, [the transferrer] became subject to the individual liability prescribed by the statute. This liability attached to him until, without fraud as against the creditors of the bank for whose protection the liability was imposed, he should relieve himself from it. He could do so by a *bona fide* transfer of the stock. But where the transferrer, possessed of information showing that there is good ground to apprehend the failure of the bank, colludes and com-

[1] Young *v.* McKay, (1892) 50 Fed. Rep. 394, following Whitney *v.* Butler, 118 U. S. 655; s. c., 7 Sup. Ct. Rep. 61. The court distinguished Richmond *v.* Irons, 121 U. S. 27; s. c., 7 Sup. Ct. Rep. 788.

bines, as in this case, with an irresponsible transferee, with the design of substituting the latter in his place, and of thus leaving no one with any ability to respond for the individual liability imposed by the statute, in respect of the shares of stock transferred, the transaction will be decreed to be a fraud on the creditors, and he will be held to the same liability to the creditors as before the transfer. He will be still regarded as a shareholder *quoad* the creditors, although he may be able to show that there was a full or a partial consideration for the transfer, as between him and the transferee. The appellees contend that the statute does not admit of such a rule, because it declares that every person becoming a shareholder by transfer succeeds to all the liabilities of the prior holder, and that, therefore, the liabilities of the prior holder, as a stockholder, are extinguished by the transfer. But it was held by this court in National Bank *v.* Case, 99 U. S. 628, that a transfer on the books of the bank is not in all cases enough to extinguish liability. The court in that case defined as one limit of the right to transfer that the transfer must be out and out, or one really transferring the ownership as between the parties to it. But there is nothing in the statute excluding, as another limit, that the transfer must not be to a person known to be irresponsible, and collusively made with the intent of escaping liability and defeating the rights given by statute to creditors. [The transferee here] might be liable as a shareholder succeeding to the liabilities of [the transferrer], because he has voluntarily assumed that position; but that is no reason why [the transferrer] should not, at the election of creditors, still be treated as a shareholder, he having, to escape liability, perpetrated a fraud on the statute. This is the view enforced by the decision of the chief justice in Davis *v.* Stevens, 17 Blatchf. 259."[1]

§ 365. **When a transfer of shares does not relieve the stockholder.**— In a case before the United States Supreme Court it appeared that a stockholder claimed that he had sold his stock, one hundred and fifty shares, about seven months before the resolution of the directors to go into voluntary liquidation; fifty shares about three months before, and fifty shares on or about the date of the passage of that resolution, and that he was not liable. The stock books of the bank showed a transfer of the

[1] Bowden *v.* Johnson, (1882) 107 U. S. 251, 261 262.

shares partly on the last date, and partly afterwards. The court sustained the decree against him by the Circuit Court.[1]

§ 366. **Liability of stockholder survives.**—There has been a case before the Supreme Court of the United States, a bill filed by the creditors of a national bank which had by resolution of its directors gone into voluntary liquidation to enforce the statutory liability of the stockholders, in which the court passed upon and determined several questions raised in the case. One question raised upon the appeal of one of the respondents, who had been appointed after the institution of the suit an administrator *de bonis non* of one of the original defendant stockholders, was upon the contention of this administrator that the personal liability of his intestate did not survive as against the adminis-

[1] Richmond *v.* Irons, (1887) 121 U. S. 27. Mr. Justice MATTHEWS, speaking for the court, said: "As to the fifty shares of stock sold by [appellant] to the president of the bank [on the day of the adoption of the resolutions for liquidation], we think the conclusion cannot be resisted that the transaction was made in contemplation of the insolvency of the bank, and although both parties may have believed that the bank would ultimately be able to pay all of its debts notwithstanding this transaction, we think that, as against creditors, it was fraudulent in law, and to that extent [appellant] is chargeable as a shareholder. The sale of [the shares held previously] there is no reason to suppose were not made in entire good faith, and without any expectation on the part of the parties of the insolvency of the bank. Notwithstanding that, [appellant] continued to be upon the books of the bank the owner of the shares until [the date of the action of directors looking to liquidation of the bank], and the day after, when they were * * * transferred. By § 5139 of the Revised Statutes, those persons only have the rights and liabilities of stockholders who appear to be such as are registered on the books of the association, the stock being transferable only in that way. No person becomes a shareholder, subject to such liabilities, and succeeding to such rights, except by such transfer; until such transfer, the prior holder is the stockholder for all the purposes of the law. It follows, therefore, that [appellant], in respect to the shares [previously] sold by him, was the statutory owner on the day [of the passage of the resolution]. His liability as such stockholder is the same as if he had that day sold and transferred the stock to [the president], but such a sale and transfer could only have been made by [appellant], who was himself a director, in contemplation and actual knowledge of the suspension of the bank; it would operate as a fraud on the creditors, an effect which the law will not permit. The case is not within the rule laid down in Whitney *v.* Butler, 118 U. S. 655. Here there is no proof, as there was in that case, of the delivery of the certificates to the bank, and a power of attorney authorizing its transfer, with a request to do so, made at the time of the transaction. The delivery was to [the purchaser], not as president, but as vendee."

trator, and that, therefore, no decree could be rendered against him subjecting the estate of his intestate in his hands for administration to the liability under the statute. The court held that such a decree could be rendered.[1] In a very late action in a federal court by a receiver of an insolvent national bank against the executors of a deceased shareholder, a portion of his shares of stock having been redeemed from the pledgee of the same by paying the debt for which it was pledged and these shares issued to them as executors, to recover an assessment made upon shareholders, the executors took this among their positions with reference to the right to recover, that no claim existed against the estate; that when testator died, the bank was then a going concern, and his liability to be assessed upon the shares of stock owned by him was merely a contingency, and that his estate in the hands of the executors could only be subject to the payment of such demands as were existing claims at the time of the death of the testator. The court held adversely to this contention and rendered a decree holding the estate liable.[1]

[1] Richmond *v.* Irons, (1887) 121 U. S. 27. Mr. Justice MATTHEWS, for the court, said: "The judicial decisions more directly relied upon by the appellant in support of [his] contention are those of Dane *v.* Dane Manufacturing Co., 14 Gray, 488; Bacon *v.* Pomeroy, 104 Mass. 577; Ripley *v.* Sampson, 10 Pick. 371; Bangs *v.* Lincoln, 10 Gray, 600; Gray *v.* Coffin, 9 Cush. 192. These cases, however, so far as they are in point, are based upon the particular language of the statutes of Massachusetts, materially differing from that contained in the National Banking Act. Under that act the individual liability of the stockholders is an essential element in the contract by which the stockholders became members of the corporation. It is voluntarily entered into by subscribing for and accepting shares of stock. Its obligation becomes a part of every contract, debt and engagement of the bank itself, as much so as if they were made directly by the stockholder instead of by the corporation. There is nothing in the statute to indicate that the obligation arising upon these undertakings and promises should not have the same force and effect, and be as binding in all respects, as any other contracts of the individual stockholder. We hold, therefore, that the obligation of the stockholder survives as against his personal representatives. Flash *v.* Conn, 109 U. S. 371; Hobart *v.* Johnson, 19 Blatchf. 359. In Massachusetts, it was held in Grew *v.* Breed, 10 Met. 569, that administrators of deceased stockholders were chargeable in equity, as for other debts of their intestate, in their representative capacity."

[1] Wickham *v.* Hull, (1894) 60 Fed. Rep. 326. SHIRAS, D. J., said: "The liability to respond to assessments made upon the capital stock is purely statutory in its origin, and the extent and nature of the obligation is determined by the provisions of the statute creating the same. Section 5151 of the Revised Statutes enacts that 'the shareholders of every national banking

§ 367. Liability of a married woman upon shares of stock held by her in her own right.— The shareholder who was being sued for an assessment ordered by the comptroller of the currency upon the shareholders of this national bank, being a married woman, contended that the coverture, at the time of the transfer of stock to her, as well as when the bank failed, protected her against assessment upon the stock paid in her name

association shall be held individually responsible, equally and ratably, and not one for another, for all contracts, debts and engagements of such association, to the extent of the amount of their stock therein, at the par value thereof, in addition to the amount invested in such shares.' Under the provisions of this section, there existed a personal liability against [the testator] for all contracts, debts and engagements of the bank in force at the date of his death. After his death, no additional liability could be created against [testator] personally by the creation of new debts or obligations on part of the bank. Provision for such cases is made in section 5152, Revised Statutes, in which it is enacted that 'persons holding stock as executors, administrators, guardians or trustees, shall not be personally subject to any liabilities as stockholders, but the estates and funds in their hands shall be liable in like manner and to the same extent as the testator, intestate ward or person interested in such trust funds would be if living and competent to act and hold the stock in his own name.' Upon the death of a stockholder, the legal title of the shares may pass to his executor or administrator, but the liability for the debts of the bank does not follow the transfer of the title to the executor or administrator, but the statute declares that the liability for the debts shall attach to the estate of the deceased. In other words, the estate is put in the place of the deceased owner, and the statutory liability will exist against the estate and not against the executor individually. In Richmond *v.* Irons, 121 U. S. 27–55; s. c., 7 Sup. Ct. Rep. 788, it was contended that the personal liability of the intestate for assessments upon the capital stock did not survive as against an administrator, nor as against the funds of the estate in his hands; but this contention was overruled, it being held that, under the provisions of the National Bank Act, 'the individual liability of the stockholders is an essential element in the contract by which the stockholders became members of the corporation. There is nothing in the statute to indicate that the obligation arising upon these undertakings and promises shall not have the same force and effect and be as binding in all respects as any other contracts of the individual stockholder. We hold, therefore, that the obligation of the stockholder survives as against his personal representatives.' Under the ruling of the Supreme Court in that case, if, at the time of the death of [this testator], there existed a personal liability against him, under the provisions of section 5151, Revised Statutes, such liability would survive against his executors; and if the liability was created after his death, and while the shares of stock formed part of his estate, then, under the provisions of section 5152, the estate became responsible for such liability, and under either state of facts a claim would exist against the estate."

upon the books of the bank. The Supreme Court of the United States held that a married woman in the District of Columbia, of which she was a resident at the time of these transactions, might become a holder of stock in a national banking association, and assume all the liabilities of such a shareholder, although the consideration might have proceeded wholly from her husband; also, that the coverture of a married woman who was a shareholder in a national bank did not prevent the receiver of a bank from recovering judgment against her for the amount of an assessment levied upon the shareholders equally and ratably under the statute.[1] Applying the provision of the Code of North Carolina, that no woman during coverture shall be capable of making any contract to affect her real and personal estate without the written consent of her husband, in a suit by a receiver of a national banking association against a married woman to recover an assessment made upon the stockholders by the comptroller of currency, it was held that a purchase of stock in a bank by a married woman was not a "contract" within the terms of the statute, and

[1] Keyser *v.* Hitz, (1890) 133 U. S. 138; s. c., 10 Sup. Ct. Rep. 290. The court, speaking through Mr. Justice HARLAN, referred to the case of the Reciprocity Bank, 22 N. Y. 9, 15, which involved the liability of a married woman as a shareholder in a state bank, as instructive. It was said: "The Constitution and statutes of New York made the shareholders in corporations and joint-stock associations for banking purposes, issuing bank notes, 'individually responsible,' etc. The Court of Appeals of that state, speaking by Chief Justice COMSTOCK, said: 'It is also said that *femes covert* are not liable to suit or judgment at the common law, and in general this is true. It is also true that the apportionment of liability among stockholders in banks, when duly confirmed, becomes a judgment against each stockholder, to be enforced by execution as in other cases. But it was competent for the legislature to depart from this rule and analogies of the common law, and to make married women and their estates liable in this proceeding as other stockholders in banks are made liable. This, we think, has been done, and it seems to us proper to add that we see no reason why it ought not to be done, in order to effectuate the policy on which the constitutional provision and the statute are founded. It might go far to defeat the policy if married women could take and hold stock without liability to the creditors.' See, also, Sayles *v.* Bates, 15 R. I. 345. This question arose in Anderson *v.* Line, in the Circuit Court of the United States for the eastern district of Pennsylvania, where it was held by Judge McKENNAN that a married woman was not exempted by reason of her coverture from the liability imposed by congress upon shareholders in national banks. 14 Fed. Rep. 405. To the same effect is the decision of Judge WHEELER in Witters *v.* Sowles, 32 Fed. Rep. 767."

that the wife was liable upon the assessment, although the stock was purchased without the written consent of her husband.[1]

§ 368. **Rules as to actions to enforce liability of stockholders.**— One becoming a stockholder in a national bank thereby submits himself to the provisions of the National Bank Act, and becomes liable to be assessed to the extent of his statutory liability for all debts of the bank existing while he holds his stock.[2] An assessment made upon stockholders of a national bank for the payment of the debts of the bank may be collected by the receiver by an action at law against the stockholders; and in such an action the stockholders cannot inquire into the legality of the receiver's appointment. Furthermore, in such an action the complaint need only allege that the comptroller determined that the assessment was necessary and levied it, as such an assessment by the comptroller is conclusive against the stockholders.[3] In an action of this kind, the fact that defendant's name appears on the subscription list of the corporation, and that he paid assessments on the stock subscribed, are sufficient evidence that he was a stockholder.[4] Actions by a receiver of a national bank against stockholders for assessments on the stock are subject to the state Statutes of Limitations.[5] A decree on a creditor's bill taken against a stockholder of a national bank, on the basis that his shares of stock bore to the whole stock of a bank, has been held by the Illinois Supreme Court not to be erroneous.[6]

[1] Robinson *v.* Turrentine, (1894) 59 Fed. Rep. 554.

[2] Young *v.* Wempe, (1891) 46 Fed. Rep. 354.

[3] Ibid. See, as sustaining the text, Kennedy *v.* Gibson, 8 Wall. 498; Casey *v.* Galli, 94 U. S. 673; Bank *v.* Case, 99 U. S. 628; Bailey *v.* Sawyer, 4 Dill. 463; Strong *v.* Southworth, 8 Ben. 331; Stanton *v.* Wilkeson, 8 Ben. 357; Welles *v.* Stout, 38 Fed. Rep. 67; Richmond *v.* Irons, 121 U. S. 27; s. c., 7 Sup. Ct. Rep. 788.

[4] Glenn *v.* McAllister's Exrs., (1891) 46 Fed. Rep. 883; Turnbull *v.* Payson, 95 U. S. 418; Glenn *v.* Springs, 26 Fed. Rep. 494; Vanderwerken *v.* Glenn, 85 Va. 9; s. c., 6 S. E. Rep. 806; Glenn *v.* Orr, 96 N.C. 413; s. c., 2 S. E. Rep. 538.

[5] Butler *v.* Poole, (1890) 44 Fed. Rep. 586.

[6] Wheelock *v.* Kost, (1875) 77 Ill. 296. See Pollard *v.* Bailey, 20 Wall. 520.

CHAPTER XV.

OFFICERS OF NATIONAL BANKS—CRIMINAL ACTS.

§ 369. Misapplication of funds by officers.
370. Making "false entries" in reports, etc.
§ 371. Improper certification of check.
372. Restrictions of Banking Law of New York upon banks and their officers.

§ 369. Misapplication of funds by officers.—BENEDICT, D. J., has held, in the prosecution of the president of a national bank for misapplication of its funds, that the indictment alleging that he "unlawfully and willfully, and with intent to injure and defraud the said association, for the use, benefit and advantage of himself, did misapply certain of the money and funds of said association, which he * * * then and there, with the intent aforesaid, paid, and caused to be paid," to certain persons named, was bad for failure to allege the facts that made such payment unlawful or criminal.[1] And it is not essential that an indictment in such a case should allege that the acts charged were done without the knowledge and assent of the directors of the association, for such knowledge and assent would not relieve the president from liability for an unlawful or continual misappropriation of the bank's funds.[2] These rules have been declared by the United

[1] United States *v.* Eno, (1893) 56 Fed. Rep. 218. It was said: "The law controlling on this occasion has been settled by the Supreme Court of the United States. The only duty devolving upon this court in this case is to apply that law to the indictment found against the defendant. By the law declared by the Supreme Court in Britton's Case, 107 U. S. 669; s. c., 2 Sup. Ct. Rep. 512, an indictment for a misapplication of the funds of a national bank must specify the particulars of the appropriation, so as to show the application charged to be a criminal misapplication as distinguished from applications that are unlawful but not criminal. There must be averments to show how the application was made, and that it was an unlawful one." And in Northway's Case, 120 U. S. 332; s. c., 7 Sup. Ct. Rep. 580, it is said by the Supreme Court: "It is of the essence of the criminality of the misapplication that there should be a conversion of the funds to the use of the defendant, or of some person other than the association."

[2] United States *v.* Eno, (1893) 56 Fed. Rep. 218, 220. It was said: "The statute does not make absence of authority from the directors an ingredient in the crime of misapplication. I conceive that a conversion of the funds of a national bank by its president may be a criminal misapplication of the funds of the bank, although done with the knowledge and assent of the directors

States Supreme Court as to indictments of national bank officers under the Revised Statutes of the United States, section 5209: In such an indictment, for willfully misapplying the funds of a national bank, it is not necessary to charge that the moneys and funds alleged to have been misapplied had been previously intrusted to the defendant; since a willful and criminal misapplication of the funds of the association may be made by its officer or agent without having previously received them into his personal possession. In charging in an indictment the president of a bank with aiding and abetting its cashier in the misapplication of the funds of the bank, it is not necessary to prove that he then and there knew that the person so aided and abetted was the cashier. An indictment which charges in substance that the defendant was president and agent of a certain national bank theretofore duly organized and established, and then existing and doing business, under the laws of the United States, and that being such president and agent, he did then and there "willfully and unlawfully, and with intent to injure the said national banking association, and without the knowledge and consent thereof, abstract and convert to his own use certain moneys and funds of the property of the said association of the amount and value," etc., sufficiently describes and identifies the crime of abstracting the funds of the bank created by the section of the Revised Statutes above referred to. An indictment which charges that the defendant "was then and there president and agent of a certain national banking association, to wit, [naming the association], theretofore duly organized and established and then existing and doing business at [naming the place], under the laws of the United States," sufficiently states that that bank was organized under the National Banking Act, or to carry on the business of banking under a law of the United States.[1]

§ 370. **Making "false entries" in reports, etc.**—The offense of making false entries on the books of a national bank,

of the bank. The president of a national bank is not the association, nor are the president and directors the association. They are only officers of the association. The moneys of the stockholders and of the depositors in the association are not the moneys of these officers, but of the association, and it has not yet been held that a national bank may be pillaged of such moneys by its president with impunity, provided the act be done in pursuance of a conspiracy between the president and the directors, or a majority of them."

[1] United States *v.* Northway, (1887) 120 U. S. 327.

for which an officer of the bank is subject to indictment for and punishment under the United States Revised Statutes, section 5209, it not being a crime of which the state courts have concurrent jurisdiction under the United States Revised Statutes, section 5328, is exclusively cognizable by the federal courts.[1] A president of a national bank was indicted for aiding and abetting in the making of false entries and also for making false entries in the books of the bank with intent to injure, deceive, or defraud, etc., under Revised Statutes of the United States, section 5209, in the northern district of Illinois. BLODGETT, J., of the United States Circuit Court, held that such entries must be willfully and intentionally false, and that mere clerical mistakes or an arbitrary exercise of discretion in keeping the books, not amounting to an abuse thereof, were insufficient to constitute the offense. That, under charge of the indictment of making false entries in a report to the comptroller of the currency, it was no defense that such entries were made by a clerk and verified by the president without actual knowledge of the truth, it being his duty to inform himself, and especially in this case as regarded items showing assets and liabilities. That under the charge of making false entries in this report to the comptroller of the currency, with the intention to injure and defraud the banking association and the stockholders thereof, and to deceive its directors, it was not sufficient to prove an intent to deceive other persons, such as creditors, depositors, the comptroller, or the public. That the testimony of a bank examiner, who was a skilled accountant, was admissible to show false entries; but that it must consist of knowledge derived from his investigation of the books, and not of conclusions based partly upon statements of officers and clerks of the bank. The rule prescribed for the jury as to determining the president's guilty intent was that they should consider his relation to the bank as an officer and a shareholder, assistance given the bank by him in its embarrassment by the loan of his individual money, and whether he had any motive for making false entries, together with circumstances that may have induced him to do so, such as an examination by the officers of the bank's affairs at the time the entries were made; and, where the president's fraudulent intent was not sufficiently shown, evidence of his good character would resolve the doubts in his favor,

[1] In re Eno, (1893) 54 Fed. Rep. 669, following Bank *v.* Dearing, 91 U. S. 29.

but not if his guilt was conclusively proven.[1] HAMMOND, J., of the United States Circuit Court for the southern district of Ohio, has declared the following rules in the prosecution of officers of a national bank for the offense of making false entries, under section 5209 of the Revised Statutes of the United States, to wit: Directors of a national bank are "officers" within the meaning of this section which makes it a misdemeanor for bank officers to make false entries in any book, report or statement of the bank, with intent to deceive any of its officers. Under the statute, intention to deceive any one director or officer is as criminal as the intention to deceive all of them. A conviction cannot be had under the statute where it appears that the officers alleged to have been deceived were accomplices in the speculation, to hide which the false entries were made. If such false entries had a natural tendency to deceive the bank officers, the fact that defendants deny having had any such actual intent cannot rebut the presumptions of intent arising from the nature of the entries themselves. In such case the fact that the officers in question were not actually deceived is not conclusive proof of the absence of intent to deceive.[2] It has been held in the United States District Court for the eastern district of Pennsylvania that false entries in a statement, made by a bookkeeper of a national bank at the request of the bank examiner, purporting to give the balances due depositors, which statement it was the duty of the examiner to make and not of the bookkeeper, would not sustain an indictment for making "false entries in * * * a statement of the association," under Revised Statutes United States, section 5209.[3] The indictment of certain of the officers of a national bank for making "false" entries, etc., in violation of United States Revised Statutes, section 5209, charging the directors with making false entries in a report to the comptroller of the currency on the condition of the bank, PUTNAM, Circuit Judge, held could not be sustained under that section, as under United States Revised Statutes, section 5211, the sole duty of the directors

[1] United States *v.* Allen, (1880) 47 Fed. Rep. 696.

[2] United States *v.* Means, (1889) 42 Fed. Rep. 599. As to what was a sufficient indictment against the president of a national banking association for making false entries in book, report or statement of such association under section 5209 of the Revised Statutes of the United States, see United States *v.* Hughitt, (1891) 45 Fed. Rep. 47.

[3] United States *v.* Eqe, (1892) 49 Fed. Rep. 852.

in regard to the reports to the comptroller is to attest them by their signatures; and entries by the directors would be mere spoliation and "false" within the meaning of section 5209. As to certain technical objections to the indictment for this offense, it was held that the use in the indictment of the words "them and others," in alleging that the defendant was president or director of such bank, and that he made alleged false entries, was not uncertain or repugnant merely because in one place the words might in one place refer to the whole of a day and in another to only one instant of the day; also, that the omission of the signs for dollars and cents in the recitals of the alleged false entries in the reports to the comptroller, and misnomer of the reports, were immaterial where the reports were set out by their tenor in the indictment, so that those discrepancies were at the most mere "matter of form" within the meaning of United States Revised Statutes, section 1025, for which the indictment is not "to be deemed insufficient." And it need not be alleged specifically in an indictment for this offense that the reports were transmitted to the comptroller of the currency, or that they were published.[1] Upon a reargument of some of the questions involved in this case, PUTNAM, Circuit Judge, held that the indictment for making false entries against the president of the national bank, charging that it was done "with intent to injure and defraud the said association and certain persons to the grand jurors unknown," was sufficient so far as concerned the allegations of intent.[2] The indictment alleging that the false entries in question indicated that there was then in the paying teller's department of the bank a certain amount in gold, legal tenders and gold certificates when such amount was not there in fact, it was not necessary that the indictment should further allege that such amount was not then in other departments of the bank.[3] The indictment, in addition to the entries themselves, need set out the context only when it so modified the entries as to be, in presumption of law, a part of them. The indictment was not invalidated by the fact that the note teller's and paying teller's books, in which it was charged the president made the false entries on which the indictment was based, were usually kept by those officers without interference by

[1] United States *v.* Potter, (1892) 56 Fed. Rep. 83.

[2] Following U. S. *v.* Britton, 107 U. S. 655; s. c., 2 Sup. Ct. Rep. 512.

[3] Ibid.

the president. The court held counts charging false entries by the president in reports of the condition of the bank, which alleged that the reports were made in conformity with the law, and then set them out by their tenor, to be bad for their failure to allege specifically that the reports were verified and attested by the cashier.[1] In a case against one of the directors of this same national bank, in which he was charged with a violation of United States Revised Statutes, section 5209, relating to the making of false entries, PUTNAM, Circuit Judge, held that it was an indictable offense under that section to make a false entry in a report to the comptroller of the currency, or to aid and abet the making of such an entry. He also declined to construe an allegation in the indictment that defendant "did make a certain false entry in a certain report of the said association," to mean that the entry was made after the report was completed, and was in fact an alteration. For the purposes of the section prescribing the offense, and for an indictment drawn under it, the preparation and completion of the report to the comptroller, the making of the false entry therein, its verification, attestation and delivery to the comptroller might be considered simultaneous, and there was, consequently, he held, no repugnance in failing to allege in the indictment that any or all of these things occurred in consecutive order. And though the count in this indictment, for aiding and abetting the cashier in making the false entries, described defendant as "being then and there a director of the bank concerned," it could not be held that the counts charged him with aiding and abetting in his official character. Counts in the indictment charging the defendant with procuring and counseling the false entry before the fact were held valid, such acts being covered by the clause of the section extending the penalty to any one who "abets" an officer or agent in the acts prohibited. The entry, the tenor of which was set forth, contained the words "see schedule." It was held not to be a valid objection to the indictment that those words were not explained, it being necessary to set out the context only when it is presumptively a part of what

[1] United States *v.* Potter, (1892) 56 Fed. Rep. 97. The court reviewed the cases of U. S. *v.* Britton, 108 U. S. 193; s. c., 2 Sup. Ct. Rep. 526; Claassen *v.* U. S., 142 U. S. 140; s. c., 12 Sup. Ct. Rep. 169; U. S. *v.* Eqe, 49 Fed. Rep. 852; U. S. *v.* Northway, 120 U. S. 327; s. c., 7 Sup. Ct. Rep. 580; Cross *v.* North Carolina, 132 U. S. 131; s. c., 10 Sup. Ct. Rep. 47.

is set out. In such a case it is sufficient for the indictment to allege the substance of the reports to the comptroller, for whether they are such reports as the law requires can be determined by the court from the allegations that they were made in response to the comptroller's order, and the allegations touching their attestation, verification and other like matters.[1] In the United States District Court for the northern district of Iowa, on the indictment of an officer of a national bank for making false entries in reports to the comptroller, the court, in its instructions to the jury, declared these rules: A "false entry" in a report by national bank officers or directors to the comptroller, within the meaning of Revised Statutes United States, section 5209, is not merely an incorrect entry made through inadvertence, negligence or mistake, but is an entry known to the maker to be untrue and incorrect, and by him intentionally entered, while so knowing its false and untrue character. A national bank is not required to conform the headings of the various accounts on its books to any prescribed names, nor to the names stated in the form of report prescribed by the comptroller; and, therefore, when a report is called for, if the person making it enters under the headings in the prescribed form a statement of the bank's condition, which is true in respect to the headings in said form, he has fulfilled the demands of the law. The entry of "Loans and Discounts" in reports to the comptroller does not guarantee the solvency of the makers of the paper, but is a statement that in truth and fact at the date named in the report the bank actually held and owned "loans and discounts" to the aggregate so reported. It is not making a "false entry" within the meaning of the statute, to enter in such report, under heading of "Loans and Discounts," items which, on books of the bank, and for convenience of its officers, have been temporarily withdrawn from that heading, and which are, from day to day, carried on books of the bank under heading of "Suspended Loans," while awaiting action of directors as to same being withdrawn from character of loans, and entered up as a loss on "Profit and Loss" account.[2] In determining whether the entry, under heading of "Loans and Discounts" in such report, of certain corporation bonds which were secured by mortgage, and owned by the bank, was the making of a "false entry,"

[1] United States *v.* French, (1893) 57 Fed. Rep. 382.

[2] United States *v.* Graves, (1892) 53 Fed. Rep. 634.

within the meaning of the statute, the jury may consider the fact that on the prescribed form of report, after a heading of "U. S. Bonds," there is a heading of "Other Stocks, Bonds," etc., and that, in the report made, certain other corporation bonds, owned by the bank, in large amounts, were entered under the latter heading. Where the form of report as presented by the comptroller contains heading of "Loans and Discounts," and also of "Overdrafts," it is the duty of the bank officer to make his entries in such report in such manner that each of the headings shall truthfully state the condition of his bank as to such heading; and he is not justified in entering overdrafts which are being carried on the books of the bank as "Overdrafts" as "Loans and Discounts," merely because he regards an overdraft as a temporary, indefinite loan, nor because those two headings are both found among the "Resources" of the bank; but he should report the overdrafts which are carried on the books of the bank as "overdrafts" in the heading of "Overdrafts," and thereby correctly show the character of the bank's resources in this particular. In determining whether defendant made a "false entry," within the meaning of the statute, when he included in such report, as "Loans and Discounts" of the bank, amounts which were being carried on the books of the bank as "Overdrafts," the jury will not consider whether other national banks followed the same practice. Such practice, if it existed, would not change defendant's statutory duty; but the jury, in determining whether such entry, if a "false entry," was made with intent to deceive and defraud, may consider whatever knowledge defendant is shown to have had as to the practice of any other national bank in this respect.[1] A director of a bank is personally liable to the bank on paper made to it by a firm of which he is a member, and in making a report of the condition of the bank to the comptroller, the amount of such paper should be entered under the heading of "Liabilities of Directors (Individual and firm) as Payers;" and, in determining whether the omission of such an item from this heading was made with intent to deceive, etc., the jury may consider what effect, if any, upon defendant's action in this respect, was caused by the receipt of a letter from the comptroller, prior to the making of the report, calling the attention of the bank officials to the excessive amount of the loans made by the bank to its directors,

[1] Ibid.

and demanding immediate reduction thereof. In determining whether a certain false entry, made by a national bank officer in a report to the comptroller, was made with intent to deceive or defraud, etc., within the meaning of the statute, the jury are authorized to infer the intent, if the natural and legitimate result of such "false entry" would be to deceive any other officer or officers of the bank, or any agent appointed to examine into its affairs. It is not necessary to complete the offense of making a "false entry" in a report to the comptroller of currency of the condition of a national bank, with intent to deceive or defraud, that any person should have been in fact actually deceived, or defrauded, for the making of such a "false entry," with the intent to deceive or defraud, is sufficient.[1]

§ 371. **Improper certification of check.**— In this case the officer of a national banking association was indicted for a violation of the act of congress of July 12, 1882, chapter 290, section 13, amendatory of the United States Revised Statutes, section 5208, which makes it a misdemeanor for any officer, clerk or agent of any national banking association to "certify any check" drawn by a person who did not then have on deposit sufficient money to meet the same, PUTNAM, Circuit Judge, held that such indictment need not allege delivery of the check by the bank after the certification. The statute prohibits the certification of checks "before the amount thereof shall have been regularly entered to the credit of the drawer on the books of the banking association;" and the section of the Revised Statutes of which the statute was amendatory prohibits the certification unless the drawer "has on deposit with the association, at the time such check is certified, an amount of money equal to the amount of such check." There were counts in the indictment simply charging that the checks were certified contrary to the prohibition of the statute, and others charging that after certification the checks were authenticated by the paying teller. It was held that, inasmuch as the counts alleged the certification as an accomplished act, it would not be presumed that the authentication was any essential part of it; and it followed that it was not necessary to allege the absence of the required credit or deposit at the time the authentication was made. The indict-

[1] Ibid.

ment was held sufficient, it having charged in the language of the statute under which defendant was indicted that the drawer of the check had not on deposit, at the time it was certified, "an amount of money equal to that specified" in the check. Neither did the indictment charge two offenses in the same count by alleging in that count that the check was certified "before the amount thereof had been entered to the credit of the drawer on the books of the bank," and also at a time when the drawer did not "have on deposit an amount of money equal to" the amount of the check. He also held that an indictment against the president of the national bank for "aiding and abetting" the cashier in certifying checks under the prohibited circumstances could not be sustained, the statutes being of narrow range and directed only against the person who committed the act directly, or perhaps by so intimidating or overpowering another that the latter became the mere physical instrument of the former.[1] Upon appeal of this case to the United States Supreme Court it was held that a charge in an indictment that the defendant was president of a national bank, and, as such, on a day and at a place named, unlawfully, knowingly and willfully certified a certain check (describing it) drawn upon the bank, and that the drawer did not then and there have on deposit with the bank an amount of money equal to the amount specified in the check, has been held to sufficiently aver the offense described in the United States Revised Statutes, section 5208.[2] The United States Supreme

[1] United States *v.* Potter, (1892) 56 Fed. Rep. 83.

[2] Potter *v.* United States, (1894) 155 U. S. 438. Mr. Justice BREWER said: "The word 'certify,' as commonly understood, implies that the cheque, upon which the words of certification have been written, has passed from the custody of the bank and into the hands of some other party, and when the charge is that the defendant did unlawfully, knowingly and willfully certify a certain cheque, the import of that accusation is not simply that he wrote certain words on the face of the cheque, but that he did it in such a manner as to create an obligation of the bank in such a way as to make an instrument which can properly be called a certified cheque. And the subsequent recital, 'by then and there writing, placing and putting in and upon and over the face of said cheque the words and figures following,' etc., is not to be taken as absolutely limiting the import of the word 'certified' to the mere act of so writing, placing, etc., but as simply descriptive of the form of the certification of that which he personally did. It was not necessary to constitute the offense that he should himself deliver the cheque to some third party outside the bank, or even that he should take any part in such delivery. His offense would be complete if, after he

Court held that as it is of the essence of the offense against those acts that the criminal act should have been done willfully, a person charged with it would be entitled to have submitted to the jury, on the question of "willful" wrongdoing, evidence of an agreement on the part of the officers of the bank that it should be treated as a loan from day to day secured by ample collateral, and that for the check certified each day there was deposited each day an ample amount of cash.[1]

§ 372. **Restrictions of Banking Law of New York upon banks and their officers.**— The Banking Law of the state of New York, as amended, has placed a number of restrictions upon banks and their officers in this state. They are as follows: No corporation or banker shall make any loan or discount to any person, company, corporation or firm, or upon paper upon which any such person, company, corporation or firm may be liable, to any amount exceeding the one-fifth part of its capital stock actually paid in and surplus; but the discount of bills of exchange drawn in good faith against actually existing values, or of commercial or business paper actually owned by the person negotiating the same, shall not be considered as a part of any such loan or discount. No such corporation, nor any of its directors, officers, agents or servants, shall directly or indirectly purchase or be interested in the purchase of any promissory note or other evidence of debt issued by it for a less sum than shall appear on the face thereof to be due. Every person violating the provisions of this subdivision shall forfeit to the people of the state three times the nominal amount of the note or other evidence of debt so purchased. No president, director, cashier, clerk or agent of any such corporation, and no person in any way interested or concerned in the management of its affairs, shall, as individuals, discount or directly or indirectly make any loan upon any note or other evidence of debt which he shall know to have been offered for discount to such corporation and to have been refused. Every person violating the provisions of this subdivision shall, for each offense, forfeit to the people of the state

had written the words of certification as stated, with the intent that they should be used to create a contract on the part of the bank the actual delivery had been made by some clerk or other officer of the bank without his actual knowledge."

[1] Potter *v.* United States, (1894) 155 U. S. 438.

twice the amount of the loan which he shall have made. No officer, director, clerk or agent of any bank or savings bank shall borrow from the corporation with which he is officially connected any sum of money without the consent and approval of a majority of the board of directors or trustees thereof. Every person violating this provision shall, for each offense, forfeit to the people of the state twice the amount which he shall have borrowed. No such corporation shall make any loan or discount on the security of the shares of its own capital stock, nor be the purchaser or holder of any such shares, unless such security or purchase shall be necessary to prevent loss upon a debt previously contracted in good faith; and stock so purchased or acquired shall, within six months from the time of its purchase, be sold or disposed of at public or private sale. Every person violating the provisions of this subdivision shall forfeit to the people of the state twice the nominal amount of such stock.[1]

[1] Laws of N. Y. 1895, chap. 929, amending § 25, art. 1, chap. 689, Laws of N. Y. 1892.

CHAPTER XVI.

FISCAL MANAGEMENT—PUBLIC CORPORATIONS.

§ 373. The power of county commissioners under statutes of Nebraska as to purchase of lands for a poor farm.
374. Power of a building commission of a town in Connecticut.
375. For what purposes a board of education in Connecticut cannot use the public funds.
376. Management of school funds of the state by an auditor of a county under Indiana statutes.
377. Erroneous payments into the treasury of a county by a county treasurer under Indiana statutes—his right to recover the same.
§ 378. For what a school district may settle account of an ex-assessor.
379. The board of auditors of a town may be ordered to pay a judgment against the town for interest on its bonds.
380. The right of a de facto county treasurer to salary.
381. Payments to city official in excess of his salary may be recovered of him.
382. Compelling a ministerial officer to distribute the fund in his hands.
383. County warrants—their issue and validity—rules governing.
384. Statute of Limitations not applicable to county warrants.

§ 373. **The power of county commissioners under statutes of Nebraska as to purchase of lands for a poor farm.**—The statutes of Nebraska authorize the purchase by the county commissioners of each county of lands for a poorhouse, and further empower them "to receive donations to aid in the establishment of such poorhouse; and, also, * * * from time to time, as they shall see fit, to levy and collect a tax, not exceeding one per cent, on the taxable property in the county, and to appropriate the same to the purchase of land * * *." Parties who had sold land to a county for this purpose under a contract for part cash, and upon conveyance of the land the commissioners, to execute the note of the county and a mortgage upon the land as a security, brought action in the courts of that state to recover damages from the county for its refusal to accept a deed and execute the note and mortgage contemplated. The Supreme Court affirmed a judgment sustaining a demurrer to the petition on the ground that the contract was illegal and void, there being

no authority under the statute to execute a note and mortgage.[1] One who had made a similar contract with the county commissioners of a county in Nebraska, and had executed and delivered a deed of the lands for a poor farm, and had received in part payment notes payable at different times, with a mortgage upon the property to secure it, and one who was the holder of these notes, upon the county's failure to pay them, filed a bill in the United States Circuit Court praying a rescission of the contract and a reconveyance or a recovery of the amount due upon the notes. The relief prayed for was not granted by this court. On appeal the Supreme Court of the United States held that it was error to refuse the relief prayed for; that the complainants were entitled to recover of the county the unpaid balance or to have the contract rescinded upon the return of the money they had received from the county on account of the contract.[2] It was

[1] Stewart *v.* Otoe County, 2 Neb. 177. The court said: "There is no authority of law for the county commissioners to bind the county in the manner contemplated. They cannot give a promissory note, nor can they mortgage the property of the county. Should they formally do so, their action would be a nullity. In the purchase of land for a poor farm the authority of the commissioners of a county is very clearly set forth. The mode of raising the money and paying it over are all definitely stated. These statutes set a limit beyond which they cannot go. They are a guide not only to the commissioners, but equally so to all persons dealing with them, who must see to it that their contracts are within the boundaries thus described. * * * Here we find the authority, and, indeed, the only authority, for the purchase and payment of money for a 'poor farm' by the county commissioners; and here, too, are specially designated the money that may be used for that purpose, together with the mode of raising it. But there is not one word about mortgaging the property of the county to secure the payment of the purchase money at a given time. The statutes provide the only security that can be given. The public faith is pledged, and a tax not exceeding one per cent may be levied upon all the taxable property of the county annually, and, when collected, paid to the person entitled thereto by an order upon the treasurer of the county, payable out of the special fund."

[2] Chapman *v.* County of Douglas, (1882) 107 U. S. 348. *Arguendo*, Mr. Justice MATTHEWS, for the court, said: "In the present case * * * it was not the understanding of the parties that the vendor should await the collection of taxes, as prescribed by the statute, for the payment of the purchase money; but, on the contrary, there was an agreement for payment in a definite time, without regard to the condition of the county treasury, and for security by way of notes and mortgages. The agreement, as we have assumed, so far as it relates to the time and mode of payment, is void; but the contract for the sale itself has been executed on the part of the vendor by the delivery of the deed, and his title at law has actually passed to the county. As the agreement be-

claimed in this case that the Statute of Limitations of Nebraska barring the right to recover the title to real estate after ten years from the time it first accrued would defeat recovery on the part

tween the parties has failed by reason of the legal disability of the county to perform its part, according to its conditions, the right of the vendor to rescind the contract and to a restitution of his title would seem to be as clear as it would be just, unless some valid reason to the contrary can be shown. As was said by this court in Marsh *v.* Fulton County, 10 Wall. 676, 684, and repeated in Louisiana *v.* Wood, 102 U. S. 294, 'the obligation to do justice rests upon all persons, natural and artificial, and if a county obtains the money or property of others without authority, the law, independent of any statute, will compel restitution or compensation.' See, also, Miltenberger *v.* Cooke, 18 Wall. 421. The illegality in the contract related not to its substance, but only to a specific mode of performance, and does not bring it within that class mentioned by Mr. Justice BRADLEY in Thomas *v.* City of Richmond, 12 Wall. 349. The purchase itself, as we have seen, was expressly authorized. The agreement for definite times of payment and for security alone was not authorized. It was not illegal in the sense of being prohibited as an offense; the power in that form was simply withheld. The policy of the law extends no farther than merely to defeat what it does not permit, and imposes upon the parties no penalty. It thus falls within the rule, as stated by Mr. Pollock in his Principles of Contract, 264: 'Where no penalty is imposed, and the intention of the legislature appears to be simply that the agreement is not to be enforced, then neither the agreement itself nor the performance of it is to be treated as unlawful for any other purpose.' Johnson *v.* Meeker, 1 Wis. 436. The principle was applied in the case of Morville *v.* American Tract Society, 123 Mass. 129, 137, where it was said: 'The money of the plaintiff was taken and is still held by the defendant under an agreement which it is contended it had no power to make, and which, if it had power to make, it has wholly failed on its part to perform. It was money of the plaintiff, now in the possession of the defendant, which in equity and good conscience it ought now to pay over, and which may be recovered in an action for money had and received. The illegality is not that which arises where the contract is in violation of public policy or of sound morals, and under which the law will give no aid to either party. The plaintiff himself is chargeable with no illegal act, and the corporation is the only one at fault in exceeding its corporate powers by making the express contract. The plaintiff is not seeking to enforce that contract, but only to recover his own money and prevent the defendant from unjustly retaining the benefit of its own illegal act. He is doing nothing which must be regarded as a necessary affirmance of an illegal act.' The decision of this court in Hitchcock *v.* Galveston, 96 U. S. 341, 350, covers the very point. There a recovery was allowed for the value of the benefit conferred upon the municipal corporation, notwithstanding, and, indeed, for the reason that the contract to pay in bonds was held to be illegal and void. 'It matters not,' said the court, 'that the promise was to pay in a manner not authorized by law. If payments cannot be made in bonds because their issue is *ultra vires*, it would be sanctioning rank injustice

of the complainants. The Supreme Court held against the contention.[1]

§ 374. **Power of a building commission of a town in Connecticut.**— The town meeting of a Connecticut town voted for the appointment of a commission to determine upon a plan for an almshouse which it had determined to construct, and to secure

to hold that payment need not be made at all. Such is not the law.' This doctrine was fully recognized by the Supreme Court of Nebraska as the law of that state in the case of Clark *v.* Saline County, 9 Neb. 516, in which it adopts from the decision of the Supreme Court of California in Pimental *v.* City of San Francisco, 21 Cal. 362, the following language: 'The city is not exempted from the common obligation to do justice which binds individuals. Such obligations rest upon all persons, whether natural or artificial. If the city obtain the money of another by mistake or without authority of law, it is her duty to refund it from this general obligation. If she obtain other property which does not belong to her, it is her duty to restore it, or, if used, to render an equivalent therefor from the like obligation.' Argenti *v.* San Francisco, 16 Cal. 282. The legal liability springs from the moral duty to make restitution." The court further referred to Parkersburg *v.* Brown, 106 U. S. 487, and Crampton *v.* Zabriskie, 101 U. S. 601, as supporting their ruling in this case.

[1] Chapman *v.* County of Douglas, (1882) 107 U. S. 348. The court referred to Brewer *v.* Otoe County, 1 Neb. 373, quite at length, and then said: "But the more satisfactory answer to this defense is that none of the statutes of limitation referred to apply to the case at all. We have already seen that by the decision in Brewer *v.* Otoe County, 1 Neb. 373, it is the declared law of Nebraska that the claim against the county for the purchase money, on the supposition that the understanding had been to accept payment according to the terms of the statute, was not liable to the bar of the limitation acts. So that the obligation of the county to pay would not be extinguished by the statutory lapse of time. Now, although the right of [the vendor here] to rescind the contract and demand a re-conveyance occurred at the very date of the deed, he was not bound to exercise the right, and his cause of action did not accrue until he had made manifest his election. He had the right to treat as null that part of the contract which was illegal, and having executed it on his part, to waive performance according to its terms on the part of the county, and wait a reasonable length of time for the county to make the payment in the mode made lawful by the statute before executing his power to rescind the contract. Until that time had elapsed, and until, after that, [he] had elected to rescind, there was no existing cause of action, and consequently nothing upon which the Statute of Limitations could begin to take effect. When that reasonable time expired we have no means of determining. It would depend upon circumstances not disclosed in the record, such as the state of the county treasury, the extent of its other obligations, the value of the taxable property, and its general financial condition. There is nothing whatever to show that the

proposals and let to the lowest responsible bidders. The committee, by a majority vote, awarded the contract to persons other than the lowest responsible bidder, and a taxpayer sought by action to enjoin the selectmen of the town and the commission from entering into any contract for the construction of the almshouse, except with the lowest responsible bidder. The Supreme Court held that it was error on the part of the lower court to make the injunction permanent.[1]

§ 375. For what purposes a board of education in Connecticut cannot use the public funds.— In an action of a tax-

delay that had taken place in filing the present bill has been unreasonable. It is impossible, therefore, to say that any Statute of Limitations has ever begun to run against the cause of action, much less that its bar has become complete."

[1] Dibble *v.* Town of New Haven, (1887) 56 Conn. 199. Upon the powers of municipalities in this respect it was said by the court: "In the expenditure of money in the discharge of a governmental duty, a municipality is as an individual managing his private affairs. That is, a majority of the voters therein may determine whether it shall perform its duty as economically as it can, or with as large an outlay as it pleases, and the minority, in the absence of fraud, must submit to the action of the majority, finding its protection against unnecessary expenditure in the law of self-interest, to which all men are presumed to be in a greater or less degree obedient; and in making expenditures for such purpose the will of the municipality is a law unto itself, as is that of an individual to himself, and as little subject to judicial control; and if it appoints an agent to make contracts in its name for such purposes, a court has no greater power to restrain that agent than it has to restrain the agent of an individual. If, in the case before us, we should assume that the committee proposes to exceed the powers granted to it by the municipality, there would yet be no foundation for the injunction. Every person dealing with it must take notice of the limitations imposed upon it by the appointing vote. If with such knowledge any one undertakes to enter into a contract with it which it is without power to make, he takes nothing by his action. The municipality is not bound to him; no taxpayer is in danger of loss, and there is no occasion for judicial intervention. Again, if the committee should, in excess of its powers, in form enter into a contract with one not the lowest bidder, the municipality may, upon knowledge, when lawfully assembled for that purpose, ratify and adopt its acts, against the protest of an individual taxpayer, or against that of a minority. And if, in strict execution of power, the committee should bind the town by a contract, the town may break it, pay the consequent damages, and make the expenditure in another manner and to a larger amount. These acts of ratification or of change the minority is powerless to prevent. It results, therefore, that, unless there should be an assumption of obligation on the part of the town in due and legal form, no person has any cause of action against it, and no taxpayer is in danger of loss. After such

payer to restrain the members and officers of the board of education of a school district in Connecticut, from paying out the money of the district for the defense of a suit brought against certain members and ex-members of the board, for malicious and wrongful acts in connection with their duties as members of the board, the powers of a school district of that state in respect to expenditures of the moneys of the district was considered by the Supreme Court. It was held in this case, where the members of the board were sued for an injury to the business reputation of the plaintiffs by their refusal to entertain a bid offered by them for furnishing stationery for the district, on the ground that they had some time before dealt dishonestly with the district, that the matter was one in which the district as such had no interest and that its money could not be used for the defense of the suit.[1]

assumption there will be a legally authorized expenditure, and that no taxpayer can resist."

[1] Hotchkiss *v.* Plunkett, (1891) 60 Conn. 230. The court said, generally: "In order to justify the expenditure of money by a municipal corporation in the indemnity of one of its officers for a loss incurred in the discharge of their official duty, three things must appear: *First*, the officer must have been acting in a matter in which the corporation had an interest. *Second*, he must have been acting in discharge of a duty imposed or authorized by law. And, *third*, he must have acted in good faith. Gregory *v.* City of Bridgeport, 41 Conn. 76; Merrill *v.* Plainfield, 45 N. H. 126; Vincent *v.* Inhab. of Nantucket, 12 Cush. 103; Dillon on Mun. Corp. (4th ed.) § 219. School districts are *quasi* corporations of a public nature, with limited powers, strictly defined by statute, and they have no right to raise money by assessment and appropriate the same to purposes not within the scope of those powers, even though a majority of their inhabitants expressly vote so to raise and appropriate it. Berlin *v.* New Britain, 9 Conn. 180; West School District *v.* Merrills, 12 Conn. 438; Bartlett *v.* Kinsley, 15 Conn. 327, 335. The powers of school districts [under the Connecticut statutes are thus expressed]: 'Every school district shall be a body corporate and have power * * * to purchase, receive, hold and convey real and personal property for school purposes; to build, purchase, hire and repair school houses and supply them with fuel, furniture and other appendages and accommodations; * * * to purchase globes, maps, blackboards and other school apparatus; to establish and maintain a school library; to employ teachers, except for such time as the town may direct the school visitors to employ the teachers, and pay the wages of such teachers as are employed by the district committee in conformity to law; to pay taxes and borrow money for all the foregoing purposes * * *.' There is no authority conferred on a school district to raise money other than such as is conferred by this statute. The grant of power to raise money for the specified purposes is doubtless a prohibition of the raising of money for any other purposes." The opinion concludes with this declaration by the

§ 376. Management of school funds of the state by an auditor of a county under Indiana statutes.—The owner of real estate borrowed of the auditor of a county in Indiana money belonging to the school funds of the state, and a mortgage upon the land was given to secure it. There were changes of title to the land. One holding it paid the money due on the mortgage to the county auditor. The auditor thereupon indorsed upon the mortgage his certificate that the mortgage had been fully paid and satisfied, assigned and attested it, attached the seal of his office thereto and surrendered the notes and mortgage to the one paying it, and the latter caused the certificate of satisfaction to be duly and properly entered of record by the recorder of the county on the record of the mortgage in his office. On the same day the auditor entered on the register of loans kept by him as auditor in his office, a statement that the loan in question was fully paid and satisfied. The defendant in an action to foreclose this mortgage afterwards purchased this land, relying upon the record showing the satisfaction of the mortgage, and in good faith paid for it its full value without any knowledge whatever that the loan had not been in fact paid. The auditor, it appeared, appropriated the money to his own use and never paid any part of the same into the treasury of the county. In one place the statutes of Indiana provide that "All loans refunded and all interest shall be paid to the county treasurer, and his receipt shall be filed with the county auditor, who shall give the payer a quietus therefor and make proper entries." In another, that "Whenever the amount due on any mortgage shall be paid, and the treasurer's receipt therefor filed, the auditor shall indorse on the note and mortgage that the same has been fully satisfied, and surrender the same to the person entitled thereto, and on production of the same thus indorsed the recorder shall enter satisfaction upon the record." The contentions of the plaintiff were that the auditor had no power to enter the mortgage satisfied until the money was actually paid to the county treasurer and his receipt therefor filed with such auditor, and that an entry of satisfaction without the existence of such payment and receipt was a nullity, and was the same as a forgery, and that the office of the county treasurer and

court: "In any case it would be a very grave question whether a municipal corporation could make an indemnity to one of its own officers in any other way than by a vote in a meeting duly called for that purpose."

the office of the county auditor were public offices, and that an examination of such offices would have disclosed the fact that the mortgage had not in fact been paid, and inasmuch as the defendant did not examine these offices he was guilty of negligence and should not be protected. The Supreme Court thought the entry of satisfaction upon the school fund mortgage in question stood upon a different footing from a forged entry, saying further: "A forged entry would be without any authority whatever, while the entry under consideration is genuine, and made by an officer having authority to make it," the statute conferring such authority directly upon the county auditor. They said further: "It is true that the entry of satisfaction before the payment of the money to the treasurer was wrongful, but inasmuch as the auditor had the money in his hands ready to hand over to the treasurer there was no want of authority." [1]

[1] Slaughter *v.* State ex rel., (1892) 132 Ind. 465, 466, 467. As to the right of the defendant to rely upon the records it was said: "As a rule the evidence of title and of recorded liens is to be found in the county recorder's office. Judgments rendered in court constitute one exception to the rule. By reason of the statute, which declares that school fund mortgages shall be deemed recorded from the date of their execution, they seem to constitute another exception. Deming *v.* State ex rel., 23 Ind. 416; Stockwell *v.* State ex rel., 101 Ind. 1. The satisfaction entered by the auditor upon the mortgage was properly recorded by the county recorder, and an examination of records in his office disclosed an unincumbered title to the land in dispute. We think the [defendant] had the right to rely upon such records. The general rule is that a public officer is presumed to have done his duty, and until the contrary is shown he is presumed to have acted rightly. Mechem Public Offices & Officers, §§ 579–677. This author says: 'The law constantly presumes that public officers charged with the performance of official duty have not neglected the same, but have performed it at the proper time and in the proper manner.' § 579, *supra*. Finding the school fund mortgage satisfied by the proper county officers, the only persons who could satisfy the same, we think the [defendant] had the right to presume, without looking further, that the county auditor had proceeded regularly, and that the mortgage debt had in fact been paid to the county treasurer before such satisfaction was entered. The county auditor in the most solemn manner, attested by the seal of his office, had published to the world that the debt was paid, and the [defendant], in our opinion, was under no more obligation to make further inquiry than he would have been had the mortgage debt been payable to a private individual who had entered the mortgage satisfied. The county auditor was the agent of [the] state, clothed with power to make such satisfaction, and the state, we think, is bound by his acts. The general rule is that the state, as well as municipal corporations, is bound by the acts of its officers when they act within the

§ 377. Erroneous payments into the treasury of a county by a county treasurer under Indiana statutes — his right to recover the same.— An Indiana statute provides as follows: "Whenever it shall appear to the board doing county business in any of the counties of this state, by clear and sufficient proof, that, by reason of erroneous charges in the tax duplicate, or from any other cause, the treasurer of such county has paid and accounted to such board for more money than was justly due from him on account of county revenue, said board doing county business shall direct the auditor to credit said treasurer with the sum or sums thus improperly paid, and order the same to be refunded from the county treasury."[1] In a county treasurer's action against the county to recover certain amounts of money which he claimed to have been erroneously paid into the county treasury, the Supreme Court of that state held that the statute required that, before such an action could be brought against the county, the claim should be presented to the board of commissioners, proofs of its correctness be made to them, and the board determine the propriety of refunding the same, and make a proper order in the matter; also, that when clear and sufficient proofs were made in such a case, the board would have no right to refuse to make the order and thus end the claim. In this particular case, there being no evidence in the record that the claim of the treasurer had not been submitted to the board for its action under the statute, the court held the action maintainable and affirmed the judgment in the treasurer's favor so far as items outside of what he claimed to have erroneously paid into the county treasury on account of taxes due the state. As to those amounts paid in on account of the state, it was held that he could have no recovery from the county for them.[2]

scope of their authority." Citing Dill. on Mun. Corp. pp. 321, 322; Mechem Public Offices & Officers, § 824; Martel *v.* City of East St. Louis, 94 Ill. 67; Roby *v.* City of Chicago, 64 Ill. 447; Board, etc., *v.* City of Lincoln, 81 Ill. 156; 2 Herm. on Est. & Res. Adj. 1264; Big. on Est. (5th ed.) 598; Curnen *v.* Mayor, etc., 79 N. Y. 511; O'Leary *v.* Board, etc., 93 N. Y. 1; People *v.* Stephens, 71 N. Y. 527.

[1] R. S. Ind. § 6510.

[2] Board of Comrs. of Gilson County *v.* Tichenor, (1891) 129 Ind. 562. The court said: "[The statute] relates to county revenue only. We think it was the intention of the legislature that the county should not profit by the mistakes of its officers, by which it received into its treasury money to which it was not entitled; but there is nothing in the act from which it can be inferred that it was the legislative intent that the county should reimburse the

§ 378. **For what a school district may settle account of an ex-assessor.**— In an action against the guarantor of certain town orders which were taken in part settlement of a claim for moneys of a school district from an ex-assessor, in accordance with a resolution of the electors of the district at a legal meeting, as it seemed, authorizing a settlement with him for part cash and part in these town orders to be guaranteed by this defendant, it was contended that, if this settlement was authorized by the electors of the district at a legal meeting, still it was unauthorized by law; that it was beyond the power of the district to accept a chose in action in such settlement; that the only remedy of the school district was a suit upon the bond of the ex-assessor to collect the amount due from him. It did not appear from the record before the Supreme Court of Michigan whether the ex-assessor had ever given a bond, or whether, in case he did, he or his sureties were responsible. The court held that, in the case of a defaulting assessor, the electors of the school district might, at a regular meeting, authorize a settlement of the matter and direct that the amount due might be paid in part by township orders guaranteed by a responsible party, as was done in this case.[1]

§ 379. **The board of auditors of a town may be ordered to pay a judgment against the town for interest on its bonds.**— In the federal court for the northern district of Illinois the court awarded a peremptory mandamus to a town board of auditors that they audit and certify as a valid debt

treasurer for money paid to the state, or to the townships, or to corporations. In such funds the county has no interest, and to require it to reimburse the treasurer for such funds would render it necessary to tax the people of the county generally, on account of funds used in some particular township or municipal corporation for purely local purposes. This would be unjust, and to justify us in holding that the legislature intended such an injustice, the language of the statute should be such as to leave no reasonable doubt. The court erred in including in its judgment money paid over to the townships in various townships in [defendant] county. [Another statute] expressly provides that the treasurer shall be reimbursed out of the state treasury, and not out of the county treasury. It is true it devolves upon the board of commissioners to make the proper finding and order, but this is not a proceeding seeking a finding and order of the kind required, but is an action to recover a money judgment. The law does not contemplate a money judgment against the county for money erroneously paid into the state treasury."

[1] School District 2 of Township of Buckeye *v.* Clark, (1892) 90 Mich. 435.

against the town a judgment rendered in that court for interest upon certain bonds the town had issued to aid in the construction of a railroad.[1] One of the defenses or grounds upon which it was claimed by the respondent that a *mandamus* should not issue in this case was that the judgment was rendered for interest upon certain bonds issued by the town to aid in the construction of a railroad; and that both the Supreme Court of the state of

[1] United States ex rel. Portsmouth Savings Bank *v.* Board of Auditors of the Town of Ottawa, (1886) 28 Fed. Rep. 407. As to the duty of town boards of auditors in such matters, in his opinion, BLODGETT, J., said: "The statutes of this state [Illinois] provide that judgment against towns are a town charge, and when collected shall be paid to the person or persons to whom the same shall have been adjudged. Haines Tps. (ed. 1833) 66. The town board of auditors have no discretion to refuse to audit a valid judgment against the town, and have no power to pass in review upon a judgment recovered against the town upon the solemn adjudication of a court. Town of Lyons *v.* Cooledge, 89 Ill. 529; Supervisors *v.* U. S., 4 Wall. 444; U. S. *v.* New Orleans, 98 U. S. 381; City of Cairo *v.* Campbell, (Ill.) 5 N. E. Rep. 114." There was a contention that the case was affected by the General Statutes of Illinois, requiring the issue of an execution upon a judgment within seven years. It was said upon this point: "On the rendition of this judgment against the town it became the duty of the town board of auditors to audit it, and provide for its payment. No execution was needed, and the issue of an execution could add nothing to the plaintiff's right; and this right to have the judgment audited, and a tax levied and collected for its payment, seems to me to be a continuing right, in no way dependent on the question as to the lien of the judgment, whether an execution could issue upon it. The issue of an execution could do the plaintiff no good, as he could make no levy upon the property of the town, and collect nothing by it; and, hence, the plaintiff's right to enforce the payment in the only way in which a judgment can be enforced against a municipality, that is, by writ of *mandamus*, is in no way impaired by the lapse of seven years. The plaintiff, if this judgment were revived by a *scire facias*, would acquire no additional right against the town to that which he now has; and the judgment, if revived, would have no greater legal or moral force than it now has. I am, therefore, of opinion that the *mandamus* will lie to compel the auditing of this judgment, and the levy and collection of a tax for its payment, although more than seven years have elapsed since its rendition." In another part of the opinion it was said as to such judgments: "It has been repeatedly held by the Supreme Court of this State [Illinois] that a judgment against a municipal corporation cannot be collected by execution, and under the township organization laws of this state the townships are *quasi* municipal corporations for governmental purposes, and the property held by them is held for public purposes, which would seem to bring them within the same rule." Citing art. 9, § 12, Const. Ill.; City of Chicago *v.* Hasley, 25 Ill. 595; Town of Odell *v.* Schroeder, 58 Ill. 353; City of Paris *v.* Cracraft, 85 Ill. 294; Norton *v.* Peck, 3 Wis. 714; Rumford *v.* Wood, 13 Mass. 193; Drake *v.* Phillips, 40 Ill. 388.

Illinois and the Supreme Court of the United States had decided that such bonds were void for want of power in the town to issue the same. As to this objection BLODGETT, J., said: " * * * It seems to me sufficient to say that the questions as to the validity of this indebtedness were all raised in this suit, and this court held that the indebtedness was valid, and rendered judgment against the town. This judgment was never appealed from, and remains unreversed, and no error has been adjudged in reference to this particular case. Decisions of the Supreme Court in other suits on the same series of bonds or indebtedness do not reverse or affect this judgment. It is true that under the rulings of the Supreme Court as to the law under which these bonds were issued, it may be said that this court erred in rendering this judgment, but this judgment was conclusive until reversed for such error by an appellate court. * * * Nor do I think there is any force in the argument * * * that this judgment cannot be enforced by *mandamus*, because the town had no authority to create the debt in question, and, therefore, have no authority to levy a tax for its payment; because when the judgment was rendered against the town it became a charge against it as completely as if it had been rendered for a debt which the town had full authority to contract. After a judgment has been rendered by a court of competent jurisdiction, even if the court erred in so rendering it, the judgment is binding upon the town until it is reversed by the appellate court, and the board of town authorities have no discretion, but must audit it as a town charge. Town of Lyons *v.* Cooledge, 89 Ill. 529. * * * The moment a judgment is pronounced that moment it becomes the duty of the town to pay it, and of the town officers to see that it is paid by taking steps for the levying and collecting of a sufficient tax; and the town officers cannot, after judgment, be heard to question the validity of the indebtedness for which the judgment was rendered." [1]

§ 380. **The right of a de facto county treasurer to salary.**— One, in a contest as to whether he was elected county treasurer of a Nebraska county, a decision being rendered against him, appealed to the District Court. In the meantime, pending the

[1] United States ex rel. Portsmouth Sav. Bank *v.* Board of Auditors of Town of Ottawa, (1886) 28 Fed. Rep. 407, 410.

appeal, his opponent in the contest went into possession of the office, and was paid the salary and fees during his incumbency by the county authorities. This opponent was finally, by writ of ouster, removed, and the one held to have been rightfully elected placed in office. On the expiration of his term the latter retained, in settlement with his successor, a sum of money equal to what his emoluments during the period for which his opponent was in possession of the office would have amounted to. The Supreme Court of Nebraska, on a petition for a writ of *mandamus* to compel him to pay this amount to his successor as county treasurer, ordered the writ to issue, holding that the county was protected in the payment of the emoluments of the office to the *de facto* officer by its board of commissioners for the time he was in possession of the office.[1]

[1] State ex rel. Greeley County *v.* Milne, (1893) 36 Neb. 301. The court said: "The question presented for determination is whether a *de jure* county officer can recover the salary or compensation which attaches to the office while it is in the possession of an officer *de facto*, who, before any judgment of ouster has been rendered against him, has been paid by the county the salary of the office. The question has never been passed upon by this court, and the decisions in other states are conflicting and irreconcilable. In establishing a precedent we shall adopt the rule which to us seems the best supported by reason and in harmony with judicial principles. The doctrine that the acts of an officer *de facto* are void so far as they affect third parties and the public, is so familiar and well settled that no citation of authorities is necessary to show it. The acts of such officer are sustained upon the ground that to question them would devolve upon every person transacting business with the officer the duty of determining for himself, at his peril, the right of the incumbent to the office he holds. Third parties assume no such risk. They are not bound to know that the person exercising the functions of a public office under color of authority is rightfully in possession of the office, but are warranted in recognizing him as the legal and valid officer, and are justified in dealing with him as such. If a person pays to a *de facto* officer the fees allowed by law for his services, he is protected, and will not be compelled to pay them the second time to the officer *de jure*. We think the same principle should govern in a case like the one at bar. Cashman was the *de facto* county treasurer of Greeley county, and performed the duties of the office under color of title from January 9, 1890, to October 28, 1891, during which time he received all the emoluments which attached to the office. He took possession of the office in good faith by virtue of the decision in his favor of the contest court, and continued to occupy the office until the respondent was declared to be entitled to the same by virtue of a judgment of ouster obtained by him against Cashman on the final determination of the appeal in the contest case by the District Court. The county board, in settling with Cashman, and allowing him the fees and salary provided by law for the

§ 381. Payments to city official in excess of salary may be recovered of him.— A city in the state of Washington, as it was empowered to do, fixed by ordinance the salary of members of its council. Afterwards the council ordered and there was paid to a member of the council additional sums of money in excess of the salary named for services. The city brought its action against him to recover the money which it held was paid him illegally and without authority. The Supreme Court of the state held that such an order by the council was unauthorized and that the city was entitled to recover the money thus improperly paid to this member of the council.[1] The principle of law that

period during which he performed the duties of the office, the same having been made before the respondent came into possession, had no right to rely upon the apparent title of Cashman, and to treat him as an officer *de jure*. The board was justified in allowing him the emoluments of the office upon that assumption, and the county cannot be compelled to pay them again. We are aware that courts of high authority have sustained the contrary doctrine, but the decided preponderance of authorities support the conclusion we have reached." The court cited: Steubenville *v.* Culp. 38 Ohio St. 18; Wayne County *v.* Benoit, 20 Mich. 176; Parker *v.* Supervisors of Dakota County, 4 Minn. 59; Dolan *v.* Mayor, 68 N. Y. 274; McVeany *v.* Mayor, 80 N. Y. 185; Terhune *v.* Mayor, 88 N. Y. 247; Hagan *v.* City of Brooklyn, 126 N. Y. 643; Saline County *v.* Anderson, 20 Kans. 298; Gorman *v.* Boise County, 1 Idaho, 655; Shaw *v.* County of Pima, (Ariz.) 18 Pac. Rep. 273; State *v.* Clark, 52 Mo. 508; Westberg *v.* City of Kansas, 64 Mo. 493; Shannon *v.* Portsmouth, 54 N. H. 183.

[1] City of Tacoma *v.* Lillis, (1892) 4 Wash. St. 797. The court said: "It may be stated as a general legal proposition that valid ordinances have the force of laws, and are as binding upon the inhabitants of a municipality as are the statutes of the state upon its citizens generally. 1 Dill. Mun. Corp. (4th ed.) § 308; Milne *v.* Davidson, 5 Mart. (N. S.) 409. When the city council passed that ordinance they established the law upon the subject of salary of councilmen, and they were as firmly bound by its provisions as if it had been a law passed by the legislature of the territory. And this being so they had thereafter no right or authority to pay themselves any other or greater sum for services rendered in their official capacity than that specified in the ordinance so long as it remained in force. But it is argued * * * for appellant that the city council were not prohibited, either by law or by the organic act of the territory, from changing an officer's salary or fees at any time they saw proper to do so, either by ordinance or resolution, and that they did so in this case. Undoubtedly the law-making body of the corporation had, prior to the taking effect of the State Constitution, the right and power to increase or diminish the salary of appellant. The right to pass ordinances implies the right to repeal them; but in this instance we nowhere find in the record that the council ever attempted to change or appeal [repeal?] the ordinance fixing the salary of its members. It can hardly be said that the receiving and paying of claims for services alleged to have

money voluntarily paid, with full knowledge of the facts and without fraud or duress, could not be recovered from him, which was invoked by the one receiving the money in excess of his salary, the court considered inapplicable to the case.[1]

§ 382. Compelling a ministerial officer to distribute the fund in his hands.— The law as to the proper proceeding against a ministerial officer holding a fund in his hands to compel a proper distribution of it, has been declared in a case before the Supreme Court of Indiana; a petition for a writ of *mandamus* to compel a public officer here, the drainage commissioner, to pay the petitioner a sum due him on the performance of his contract in construction of a public ditch, under the laws of that state as to drainage, etc. ELLIOTT, J., for the court, said: "The case is that of a ministerial officer with money in his hands which it is his duty to pay to the party entitled to it under the law. The fund in the appellant's hands was derived from an assessment for

been rendered effected a repeal or even a modification of the ordinance, which, as we have already intimated, was the measure of the city's liability to appellant as well as of his rights to compensation."

[1] City of Tacoma *v.* Lillis, (1892) 4 Wash. St. 797. The court said: "Appellant was the agent of the city and was intrusted with the care and management of its funds, and if he appropriated any of such funds to his own use, contrary to law, he is liable therefor as such agent, although he may have done it under a claim of right and with no dishonest motive. Another reason why the doctrine contended for by counsel ought not to be held applicable to cases like the one now under consideration is that it would enable a municipal council to violate with impunity a plain provision of the Constitution. This question was before the court in Weeks *v.* Texarkana, 50 Ark. 81; s. c., 6 S. W. Rep. 504. The case was this: Weeks was city recorder, and his salary had been reduced. He claimed to be entitled to the salary as originally fixed, and sued the city to recover it. The city claimed a set-off on account of overpayment after the ordinance reducing his salary took effect. The trial court held that the money, having been voluntarily paid, could not be recovered back. The Supreme Court ruled otherwise, using this language: 'But the court below seems to have considered that the town, having voluntarily paid Weeks this salary under no misapprehension of the facts, could not recover it back. However true this may be as a general proposition, it ought not to be extended to cases where the officer so wrongfully receiving payment was a member of the council or board which ordered such payment. This would enable every municipal body to evade the salutary restraints imposed by the statute. They might vote themselves extravagant salaries after their induction into office, and when they had received the money might set the municipality at defiance.' See, also, Petersburgh *v.* Mappin, 14 Ill. 193; East Nissouri *v.* Horseman, 16 U. C. Q. B. 582; Daniels *v.* Burford, 10 U. C. Q. B. 478."

a specific purpose, and the relator, as the contractor, having constructed the ditch for which the assessments were levied, has a right to compel the appellant to distribute to him the fund as the law directs. The case before us falls within the rule that a ministerial officer who has in his hands a specific fund may be compelled by *mandamus* to make lawful distribution of the fund.[1] In this instance there is no question of contract liability; the question is as to the duty of the appellant to distribute to the relator the specific fund derived from the assessments levied to pay for the construction of the public ditch. The officer has no right to the specific fund, and he is liable, if at all, because he violates his duty in withholding the specific fund from the party entitled to it. He is not liable, upon the facts stated in the petition, to an action for a breach of contract duty, but he is liable, if liable at all, because he has violated a duty imposed upon him by law. Such cases as State ex rel. *v.* Trustees, 114 Ind. 389, are not relevant to the point here in dispute, since the liability of the appellant is not upon contract, but his liability arises out of a failure to distribute a specific fund in his hands as the law requires. Confessing, as the appellant does, by his demurrer, that he has the specific fund in his hands, and that the relator is entitled to it under the law, he cannot successfully urge as a reason for withholding the fund, that the landowners who paid the assessments which created the fund are not parties to the action. He has the fund — the assessments have been paid — and it is his duty, upon proper demand, to pay the relator the money due him out of the specific fund. There is no merit in his contention that the landowners should be parties, for nothing remains for him to do except to make proper distribution of the specific fund realized from the assessments."[2] As to the pleadings in the case, it was said: "There is a fatal defect in the petition and alternative writ. No demand is shown, and in such a case as this a demand is essential. The presumption is that an officer will do his duty upon request, and to put him in the wrong a demand is essential. Jackson School Tp. *v.* Farlow, 75 Ind. 118. A claimant of a fund cannot maintain

[1] Citing Portland Stone Ware Co. *v.* Taylor, (R. I.) 19 Atl. Rep. 1086; Board, etc., *v.* People ex rel., 24 Ill. App. 410; Case *v.* Wresler, 4 Ohio St. 561; Illinois State Hospital *v.* Higgins, 15 Ill. 185; United States ex rel. *v.* Board, etc., 28 Fed. Rep. 407; State ex rel. *v.* Board, etc., 4 Ind. 495.

[2] Ingerman, Drainage Commissioner, *v.* State ex rel. Conroy, (1891) 128 Ind. 225, 227, 228.

such an action as this without first demanding payment of his claim. The authorities are well agreed that where the duty is owing to a private person and not to the public, a demand must be alleged with precision in the petition for a writ of such an extraordinary character as that invoked by the relator." [1]

§ 383. **County warrants — their issue and validity — rules governing.**— A county in Illinois issued various county warrants upon its treasurer in favor of different parties for different considerations, which were assigned to an individual by the original payees; the assignee, in an action against the county, had judgment from the court, the trial being had upon a stipulation of facts. The appellate court, on appeal, reversed this judgment, and held that the warrants were invalid because the terms of the statute authorizing the issue of county warrants had been disregarded.[2] It was further held that neither the assignor nor the

[1] Citing State ex rel. *v.* Slick, 86 Ind. 501; Oroville, etc., R. R. Co. *v.* Supervisors, etc., 37 Cal. 354; Board, etc., *v.* Arrghi, 51 Miss. 667; State ex rel. *v.* Schaack, 28 Minn. 358; State ex rel. *v.* Davis, 17 Minn. 429; Lee County *v.* State ex rel., 36 Ark. 276; citations in 4 Am. & Eng. Ency. of Law, 106.

[2] County of Cook *v.* Lowe, (1887) 23 Ill. App. 649. The court referred to the cases, City of Springfield *v.* Edwards, 84 Ill. 626, and Chicago *v.* Shober & C. Lithographing Co., 6 Ill. App. 560, as to the rules established in these cases, and then said: "The statute in a guarded and precise manner prescribes the conditions under which warrants payable on demand, as were those on which this suit was brought, may be issued, and inhibits such issue except under such conditions, and the stipulated facts show that the warrants sued on were issued when the conditions required by the statute did not exist. The statute directs that such warrants shall be drawn and issued 'only when at, the time of the drawing and issuing of such warrants, there shall be sufficient money in the appropriate fund in the treasury to pay them,' and the stipulation admits 'that at the time of the drawing and issuing of such warrants on the county treasurer of said county there was not sufficient money in the appropriate fund in said treasury to pay them.' It was suggested in argument that the warrants were not drawn on any particular fund, but were made payable out of the treasury generally, and that there was no evidence that there was no money at all in the treasury. There is nothing in the attempted distinction. The admission that there was no money in the appropriate fund is equivalent to the statement that there was no money in the hands of the treasurer of the county liable to be drawn against by the order of the county board for the payment of the debt for which the warrants were issued. The warrants were drawn and issued without authority of law, and against the inhibition of the statute, and were, therefore, clearly invalid, and as instruments absolutely void, whether in the

assignee of the warrants could recover upon them, because they were invalid; further, that the assignee was not entitled to judgment in his favor on the void warrants, and, treating them as evidence of an assignment of the original account, he could not recover in the action as brought in his own name.[1] In an action against the board of commissioners of a Kansas county upon county warrants as to farm property, issued by the board in payment of lands purchased for a poor farm, a question was made as to whether the assessment of taxes under the statute of that state relating to the subject had been properly authorized by a vote of the people. The direct question was whether it required "a majority of all the votes cast at a poll opened for that purpose." It was held by the United States Circuit Court for the district of Kansas that it was sufficient if the proposition received a majority of all the votes cast on that particular proposition, and that it was not necessary that it should receive a majority of all the votes cast at

hands of the person to whom they were made payable, or in the hands of an assignee."

[1] County of Cook *v.* Lowe, (1887) 23 Ill. App. 649. As to the effect of the assignment of these warrants it was said by the court: "A void instrument cannot be given validity by assigning it, and while such assignment may not be entirely without operation between the parties to it, yet the void instrument can never itself be made the basis of a recovery at law or in equity. The assignment may be evidence in equity of an intention to assign the claim for which the warrant was issued. As was said in Goldsmith *v.* Stewart, 45 Ark. 153, 'although an instrument may be void, it does not follow that an assignment of it is wholly inoperative in equity. If it is supposed by the parties to represent a claim for money, and if assigned for value it will raise an equity in the assignee, not to recover on the instrument itself, but to stand in the shoes of the assignor with regard to the original claim for which it was substituted. It is evidentiary of the equity. While it is true a party to whom one of these warrants was issued, if he stood in the place of appellee as plaintiff in this suit, could have recovered the value of the services rendered or material furnished by him to the county under the common counts, his recovery would not be upon the void instrument, but on the original claim or account for which the warrant was issued. It does not at all follow, however, that the assignee can so recover; the assignment of the warrant can at best be treated as an equitable assignment of the account, and he could not sue at law upon such assigned account in his own name, but must sue, if at all, in the name of the assignor for his use. What was said in The People *v.* Johnson, 100 Ill. 537, as to county orders being transferred by indorsement, and as to the right of the assignee to sue in his own name, had reference to valid warrants. By usage and for business convenience, the assignee of such an order may sue in his own name, but is subject to all the equities and defenses which exist against the original payee. But

the election.[1] The United States Circuit Court for the eastern district of Missouri has ruled as to county warrants issued under the laws of that state, as follows: *Mandamus* having been granted requiring the County Court to draw warrants in favor of relators, payable out of "the general funds of the county," the warrants being drawn accordingly, but at relator's request, other warrants being drawn on another fund in lieu of the warrants already drawn, and issued to the relators, the latter warrants were held to have been issued pursuant to the writ of *mandamus*. That under the general statutes of Missouri, providing that county warrants are receivable in discharge of "any county or city revenue, license, tax, assessment, fine, penalty or forfeiture," such warrants were receivable in payment of a special tax levied for payment of county bonds, though the priority in which such warrants were required by law to be paid was thereby defeated. That the statute of Missouri, providing that several warrants may be issued for one claim against a county, instead of issuing a single warrant, as was provided by the existing law, did not so change the administration of county finances as to impair the remedy for the collection of outstanding warrants. And where warrants had been received from an assignee thereof in payment of taxes, and such payment had been approved by the County Court on the settlement of the accounts of the county treasurer, such payment would be considered sufficient, though this assignment was not in the form required by law.[2]

§ 384. **Statute of Limitations not applicable to county warrants.**— In a case involving the question of whether the Statute of Limitations can be pleaded successfully against county warrants, the Supreme Court of Nebraska has said, as to the holders of such: "Whoever deals with a county and takes in payment of his demand a warrant of the character of these, no

here in law appellee took nothing whatever by the assignment of the warrant."

[1] Armour Bros. Bkg. Co. *v.* Board of County Commis. of Finney County, (1890) 41 Fed. Rep. 321, supported by Commissioners *v.* Winkley, 29 Kans. 36; State *v.* Echols, 20 Pac. Rep. 523; Cass Co. *v.* Johnston, 95 U. S. 369; Walker *v.* Oswald, 11 Atl. Rep. 711; Gillespie *v.* Palmer, 20 Wis. 544; Sanford *v.* Prentice, 28 Wis. 358.

[2] United States ex rel. Huidekoper *v.* Macon County Court, (1891) 45 Fed. Rep. 400. See State *v.* Winterbottom, 123 U. S. 215; s. c., 8 Sup. Ct. Rep. 98.

time of payment being fixed, does so under an implied agreement that if there be no funds in the treasury out of which it can be satisfied, he will wait until the money can be raised in the ordinary mode of collecting such revenues. He is presumed to act with reference to the actual condition and the laws regulating and controlling the business of the county. He cannot be permitted, immediately upon the receipt of such warrant, to resort to the county to enforce payment by judgment and execution, without regard to the condition of the treasury at the time, or the laws by which the revenues are raised and disbursed." They held, therefore, that the Statute of Limitations did not apply to cases of such claims against counties; that whenever it can be shown that the funds have been collected out of which the warrants can be paid, or sufficient time has been given to do so in the mode pointed out on the statute, payment of them may be demanded, and, if refused, legally coerced.[1]

[1] Brewer *v.* Otoe County, 1 Neb. 373. The court said: "But these warrants do not, nor was it the intention of the legislature that they should, fall within the operation of this act. * * * Nor can any action rightfully be brought on such warrant until the fund is raised, or, at least, sufficient time has elapsed to enable the county to levy and collect it in the mode prescribed in the revenue laws. That the legislature never intended that county warrants should be affected by the limitation act before referred to is evident, I think, from the whole course of legislation respecting them. As late as the 12th of February, 1866, it was enacted that 'all debts heretofore incurred by the county commissioners of any county, acting in good faith, and duly recorded at the time on their books, shall be deemed valid, and the county shall be held liable for the same.' Chap. 5, § 1, Rev. Stat. Neb."

As to "Fiscal Management — Public Corporations" see further, chapter 3, "Power of Agents and Officers — Public Corporations."

CHAPTER XVII.

FISCAL MANAGEMENT — PRIVATE CORPORATIONS.

§ 385. Execution of contracts by corporations.
386. What would be conclusive of the execution of a contract.
387. Declaring dividends.
388. Rules as to declaring dividends by a mining corporation.
389. Borrowing money to pay dividends.
§ 390. Rescinding a declaration of dividend.
391. Contracts within and outside the power of private corporations.
392. Rules as to estoppel to plead that contracts are ultra vires.

§ 385. **Execution of contracts by corporations — rules governing.**— A valid written contract may be made by a private corporation in Iowa without the use of a seal, even though such contract be one out of the ordinary course of the business of the corporation.[1] There is a statute of North Carolina which prescribes that "Every contract of every corporation, by which a liability may be incurred by the company exceeding one hundred dollars, shall be in writing, and either under the common seal of

[1] Muscatine Water Co. *v.* Muscatine Lumber Co., (1892) 85 Iowa, 112. The court said: "Section 2112 of the Code contains the following: 'The use of private seals in written contracts, except the seals of corporations, is abolished.' It is argued from this that the use of private seals by corporations is governed by the rules of the common law, and that such seals must be affixed to all contracts not covering the scope of the ordinary, every-day functions of the corporations. That is not the law of this state. On the contrary, it was said in Merrick *v.* Plank Road Co., 11 Iowa, 76, that the doctrine is now well settled that corporations of all kinds may be bound by contracts not under their seals. They may make a binding contract in writing without using the seal, and so they may be held as verbal contracts; and as they may make, so they may ratify and adopt as their own, and without the use of the seal, that which has been done by another, or an officer out of the usual line of his duties." As to use of seal in corporation contracts, see Derringer's Admr. *v.* Derringer's Admr., 5 Houst. 416; Bancroft *v.* Will. Conf. Academy, 5 Houst. 577; Vandegrift *v.* Delaware R. R. Co., 2 Houst. 287. What is *prima facie* evidence that a seal was properly affixed to an instrument executed by a corporation, see Conine *v.* J. & B. R. R. Co., 3 Houst. 288. As to presumptions as to seals to contracts of corporations, see Blackshire *v.* Iowa Homestead Co., 39 Iowa, 624; Chicago, Burlington & Quincy R. R. Co. *v.* Lewis, 53 Iowa, 101; Morse *v.* Beale, 68 Iowa, 463; s. c., 27 N. W. Rep. 461; Goodnow *v.* Oakley, 68 Iowa, 25; s. c., 25 N. W. Rep. 912.

the corporation or signed by some officer of the company authorized thereto." The Supreme Court of that state have said of this statute: "This provision is important and not merely directory. Its purpose is to protect corporations against the hasty or fraudulent acts and practices of their incautious or faithless officers and agents, and as well those persons who deal with them in respect to contracts involving pecuniary liability of importance. They must necessarily act and contract by and through their officers and agents, and it is wise and salutary to protect them and those who deal with them in the way thus provided. Such contracts must be in writing and under the common seal of the corporation, or signed by some one of its officers authorized thereto. It is not sufficient to simply recognize by such officer or agent a merely verbal contract to give it efficiency. It must be done in writing, and in such way as to give evidence of the nature, purpose and substance of the contract. Otherwise, the statute would be practically nugatory. * * * The statute refers to executory contracts which create liabilities and obligations of the corporation — not to cases where they have received and availed themselves of property sold and actually delivered to them."[1] Upon an issue as to whether the execution of a mortgage by the president and secretary of a corporation was authorized by a board of its directors, in whom the control and management of its affairs was vested, parol evidence is admissible to prove the action of the board, when the record of the meeting fails to state it.[2] In the same case CALDWELL, J., said: "The omission to attach the corporate seal to the mortgages is not fatal to their validity in equity. The companies admit their execution and assert their validity. The owners of all the stock of the companies assert their validity. They were given for debts actually due from the companies to the banks. The officers and stockholders of the milling companies had no personal interest in the debts secured by the mortgages. No part of the money belonged to them, nor were any of them sureties for its payment. On this state of facts, it is not necessary to inquire whether these mortgages are legal and sufficient securities at law against the

[1] Curtis *v.* Piedmont Lumber & Mining Co., (1891) 109 N. C. 401, 403, 404.

[2] Allis *v.* Jones, (1891) 45 Fed. Rep. 148, 149; citing U. S. Bank *v.* Dandridge, 12 Wheat. 72; Mining Co. *v.* Anglo-Californian Bank, 104 U. S. 192; Eureka Co. *v.* Bailey Co., 11 Wall. 488; Whart. Ev. § 663; Davidson *v.* Bridgeport, 8 Conn. 472; Ratcliff *v.* Teters, 27 Ohio St. 66; Taymouth *v.*

general creditors of the companies. They are undoubtedly good in equity.[1] "In Koehler *v.* Iron Co., 2 Black, 716," said the court, "the court declined to treat a mortgage of a corporation not under seal as good in equity, because it was declared on as a legal, and not an equitable, mortgage." To obviate this objection the banks in this case were granted leave to amend their cross-bills by adding a special prayer, to the effect that, if the court should hold them ineffectual as legal mortgages, they may be held and treated as equitable mortgages.[2] In a late Maryland case, an action upon a contract to pay royalties executed under seal by a manufacturing corporation, the plaintiff, for the purpose of proving the execution of the agreement, offered to prove that all the persons whose names were signed thereto were stockholders of the company, and holders of all the capital stock thereof; that the board of directors consisted of three, the plaintiff, who was the president of the company, and two other parties, one of whom was its secretary, treasurer, and custodian of its corporate seal; that at a meeting of the directors the contract was signed by those two, on behalf of the company; that by authority of the board of directors at this meeting the corporate seal of the company was there and then affixed to the contract by the secretary, and that the impression of the seal used on the contract was the corporate seal of the company, adopted and used as such by it at that time; that the directors usually held their meetings for the transaction of the ordinary business of the company without making or keeping any minutes of their proceedings; and that no minutes of the meeting at which this contract was signed and sealed as aforesaid were made or kept by the company or any of its agents or officers. Upon objection the evidence was not allowed to go the jury. The Maryland Court of Appeals held the ruling to be erroneous.[3] MILLER, J., for the court said: "In our opinion it was competent for this corporation to bind itself by this contract under its corporate seal, and that the fact that it did so may be proved otherwise than by a formal resolution in writing of its board of direct-

Koehler, 35 Mich. 22; Bank *v.* Kortright, 22 Wend. 348.

[1] Allis *v.* Jones, (1891) 45 Fed. Rep. 148, 149, 150; citing Love *v.* Mining Co., 32 Cal. 639; Miller *v.* Railroad Co., 36 Vt. 452, and others.

[2] Allis *v.* Jones, (1891) 45 Fed. Rep. 148, 150.

[3] Zihlman *v.* Cumberland Glass Co., (1891) 74 Md. 303, 308, 309; s. c., 22 Atl. Rep. 271.

ors spread upon its minutes. Sealing was the essential part of the execution of this agreement by the corporation, and the essential facts to be proved are that the seal affixed to this instrument was in fact the corporate seal of the company, and that it was duly and properly affixed thereto. The offer to prove this by parol evidence is clear and satisfactory. It is that the seal affixed was the corporate seal of the company then used and adopted by it as such; that it was affixed in the presence and by the authority of the full board of directors by their secretary, who was its custodian; and that it was also signed by all the then stockholders of the corporation, and that it was signed by the [directors outside of plaintiff] for and on behalf of the company. It is hardly possible to conceive of more complete proof of the execution of a sealed instrument by a corporation than this, provided such proof may be made by parol testimony. We have already said in our opinion such testimony may be used for that purpose. The old doctrine that a corporation can bind itself by contract only by a formal resolution *in writing*, adopted by its board of directors, has long since been repudiated by the modern decisions, both in England and in this country, and no authority on that subject need be cited. We cannot distinguish this case from that of Susquehanna Bridge & Bank Co. *v.* General Ins. Co., 3 Md. 305, where the execution of a mortgage by the appellant corporation was proved by parol testimony less strong than that embraced in this offer, and where the mortgage was held valid and binding upon the corporation." In an action upon the promissory notes of a corporation it has been held in the federal court for the eastern district of Pennsylvania that an affidavit of defense that "the notes sued on do not purport on their face to have been signed by two managers of the defendant company," and that "there is no averment that the persons who signed them are or were" such managers, was not sustained where the notes were signed by the "chairman" and the "treasurer" of the corporation, inasmuch as the statute of Pennsylvania provides that the "chairman" and the "treasurer" shall be managers. It was also held that the defense that the payee of the negotiable notes, which were given in Pennsylvania, was a foreign corporation which had failed to comply with the conditions prescribed by statute to entitle it to do business in Pennsylvania, and that the contract under which the notes were given was in violation

of that statute, was not available against one who paid value for the notes before maturity, and had no notice of the illegality infecting them.[1] The promissory note sued upon here recited in the body of it, "we promise to pay," but with nothing there to indicate to whom "we" referred. It bore upon its face, in the usual place of signing, the name "John Roach," beneath which was written "Treasurer," and had in addition the impression stamped upon it of a large circular corporate seal, around the upper edge of which appeared in print, "New York Skating Rink Construction Company," and in the center of it, "Incorporated 1884," so placed that the circumference passed through the final letter of "Roach" and the word "Treasurer." The Massachusetts Supreme Court held that the note was the note of the corporation.[2]

[1] City Bank of Hartford *v.* Press Co. (Limited), (1893) 56 Fed. Rep. 260. As to formalities of contracts, see Peterson *v.* Mille Lacs Lumber Co., (Minn.) 52 N. W. Rep. 1082; Ballard *v.* Carmichael, 83 Tex. 355; Shaffer *v.* Hahn, 111 N. C. 1; s. c., 15 S. E. Rep. 1033; Ruffner *v.* Coal Co., 36 W. Va. 244; Danville Seminary *v.* Mott, 136 Ill. 289; Cary-Halidy Lumber Co. *v.* Cain, (Miss.) 13 So. Rep. 239; Teitig *v.* Boesman, 12 Mont. 404; s. c., 31 Pac. Rep. 371. What is a signature for a corporation and what will bind it, see Dwyer *v.* Rathbone, Sard & Co., 5 N. Y. Supp. 505; Davis *v.* Gemmell, 70 Md. 376; s. c., 17 Atl. Rep. 259; Saltmarsh *v.* Spaulding, 147 Mass. 224; Catlett *v.* Starr, 70 Tex. 485; Fidelity Ins., Trust & Safe Deposit Co. *v.* Shenandoah Valley R. Co., 32 W. Va. 244; s. c., 9 S. E. Rep. 180; First Nat. Bank *v.* Salem Capital Flour Mills Co., 39 Fed. Rep. 89. Agents and officers executing notes. Gane *v.* Locmo Printing Co., 46 Ill. App. 456; In re Millward-Cliff Cracker Co., 161 Pa. St. 157; s. c., 28 Atl. Rep. 1077; Elwell *v.* Puget Sound, etc., R. Co., 7 Wash. 487; s. c., 35 Pac. Rep. 376; Edwards *v.* Carson Water Co., 21 Nev. 469; s. c., 34 Pac. Rep. 381.

[2] Miller *v.* Roach, (1889) 150 Mass. 140. KNOWLTON, J., for the court, said: "The case is peculiar in the use of the corporate seal. If the words which appear on the face of the seal had been written in their place on the note and had been followed by the words, 'John Roach, Treasurer,' there would have been no doubt that they were so written as the signature of the corporation appended by its treasurer. Draper *v.* Massachusetts Steam Heating Co., 5 Allen, 338. That mode of signing is common among corporations. And if the words had been affixed in print by a stamp designed to be used in signing the corporate name, and a blank space had been left in which the treasurer's name was afterwards inserted by him in his own handwriting, the result would have been the same. We think it makes no difference that the name of the corporation impressed upon the paper was so impressed by the corporate seal, which is ordinarily used in connection with a corporate act of signing. We are of opinion that the paper should be treated as a promissory note signed with the signature of the corporation affixed by its treasurer, who, for convenience in affixing it, used a stamp,

§ 386. What would be conclusive of the execution of a contract.—The facts disclosed in this case showed a contract made by the defendant, a manufacturing corporation of Illinois, with the plaintiffs, who were advertising agents, for placing certain advertisements of the corporation. In an action brought by the advertising agents against the corporation it was proposed to place in evidence a letter from the corporation offering a compromise, which was rejected. The United States Circuit Court of Appeals for the seventh circuit held that the rejection of the testimony was error; that the execution of the contract upon which the suit was based being denied by the defendant, the letter offering to compromise the claim and making an express recognition of the contract, was admissible in evidence as an admission of the execution of the contract.[1]

§ 387. Declaring dividends.—The declaring of dividends must ordinarily be left to the sound discretion of boards of directors. Whether a corporation can safely make a dividend involves the exercise of knowledge and judgment, and the power of decid-

except in that part which contained for verification his own name and official designation." See Mann *v.* Chandler, 9 Mass. 335; Fuller *v.* Hooper, 3 Gray, 334; Carpenter *v.* Farnsworth, 106 Mass. 561; Chipman *v.* Foster, 119 Mass. 189.

[1] Scofield *v.* Parlin & Orendorff Co., (1894) 61 Fed. Rep. 804. WOODS, Circuit Judge, said: "This letter, while not admissible to prove the offer of compromise, was admissible to show an independent statement or admission of fact pertinent to the question in issue. Of the authenticity of these letters and the contract transmitted with one of them, the circumstances in proof, the regular transmission by mail, the letter heads and envelopes, and the contents of the letters themselves, leave no reasonable doubt. They should have gone to the jury, and in the absence of contrary evidence should have been accepted as conclusive of the execution of the contract by the defendant. The ruling of the court to the contrary, and presumably the sworn denial of the execution of the contract, proceeded upon the theory that in order to bind the corporation, a contract must be shown to have been executed or authorized by a formal corporate act, such as an order or resolution of a board of directors. But the business of modern mercantile and manufacturing corporations is not always or even generally conducted in that way, but is committed to agents and managers, whose powers are limited practically only to the lines of business for the prosecution of which the corporations were formed. It follows that correspondence conducted by these agents and contracts made by them in the name of the principal in the due and ordinary course of business, must be admissible in evidence as if the parties were natural persons. If a document offered against a corporation is not genuine, or its execution unauthorized, the corporation will be able in most instances to show the

ing this question should not be taken from the directors and assumed by the courts, unless it clearly appears that the directors have mistaken their legal duties. To authorize the court to intervene and decree a dividend it ought, in the first place, to appear clearly that there are surplus profits to divide, and that such profits can be separated from the necessary working capital for the purpose of a dividend, without detriment to the interest of the stockholders and the prosperity of the business of the corporation. It ought to appear that there is no good reason for withholding a division of the surplus earnings among the stockholders, and that they are withheld from the will or caprice of the directors. If there is reasonable cause for withholding the dividend then it ought not to be decreed.[1] When a board of directors, made up of experienced business men, largely interested in the welfare of the corporation, familiar with all its affairs and influenced by no improper motive, declare that a dividend cannot be made without detriment to all concerned, then the court ought to proceed with great caution in declaring a dividend, and the facts proven upon the trial ought clearly to justify such action.[2]

§ 388. Rules as to declaring dividends by a mining corporation.— It was contended in a California case that in declaring

fact, while, on the other hand, if direct proof of formal or overt corporate action or authority were required of the opposite party, it would often be, indeed, it would be, in the power of the corporation to make it difficult or impossible."

[1] Hunter *v.* Roberts, Throp & Co. (a Corporation), 83 Mich. 63.

[2] Ibid. In which case the so-called "surplus profits" appearing to be tied up in bills receivable, etc., from which the current expenses, insurance, taxes, etc., were to be obtained, the court considered evidence that a sufficient sum could not be got out of it to make any considerable dividend without great sacrifice, and not then except at the necessity of driving the corporation to add largely to its indebtedness to obtain money to carry on its business and to pay its current expenses, and held it proper to refuse to decree a dividend. As to power of trustees of a manufacturing corporation to pay dividends in New York, see People ex rel. Edison General Electric Co. *v.* Barker, (1894) 141 N. Y. 251. As to what may be distributed as dividends on stock, see Gilkey *v.* Paine, (Me.) 14 Atl. Rep. 205. As to raising money by borrowing on bond and mortgage with a view to distributing surplus among stockholders, see Coquard *v.* St. Louis Cotton Compress Co., (Mo.) 7 S. W. Rep. 176. As to dividends, see In re James' Estate, 78 Hun, 121; s. c., 28 N. Y. Supp. 992; Ford *v.* Rubber Thread Co., 158 Mass. 84; Southwestern A. & I. T. Ry. Co. *v.* Martin, 57 Ark. 355. As to dividends upon preferred stock, see McLean *v.* Pittsburgh Plate-Glass Co., 159 Pa. St. 112; s. c., 28 Atl. Rep. 211; 33 W. N. C. 459.

dividends the directors of a mining corporation had violated the Civil Code, section 309, which provides that: "The directors of corporations must not make dividends, except from the surplus profits arising from the business thereof; nor must they divide, withdraw, or pay to the stockholders, or any of them, any part of the capital stock. * * *" The contention was more fully stated in the opinion of the Supreme Court, in these words: "That the payment of the debts which the plaintiff assumed as part of the price of the property acquired from the Excelsior Water Company and the Pactolus Mining Company, as well as most of the items of expenditure for construction of tunnels, levees, ditches, etc., should be rated as current expenses and charged against its gross earnings, in order to ascertain the actual surplus profit of its business; while counsel for defendant contends, on the contrary, that the payments of the principal of its indebtedness, and its investments on what are called betterments of its property, should not be charged to current expenses of the business. As to the payment of the debts assumed by the plaintiff when it commenced business, or that incurred in making improvements, we do not understand its counsel to contend that it was necessary to pay them off before any dividends could be declared, but merely that whenever any part of its gross earnings was applied to the payment of a debt it was unlawful thereafter to replace such sum with the proceeds of a loan, and thereupon declare a dividend. The fact is not disclosed by the findings of the judge of the Supreme Court, but it seems to have been proved that in several instances money was borrowed by the plaintiff in order to pay dividends, and it seems to have happened in this way: The debts assumed by the plaintiff became due from time to time, and the permanent improvements on its property were made from time to time, so that large payments on both accounts were constantly occurring. Instead of borrowing money to make such payments at the time of making them, any money that happened to be on hand in the company's treasury was used, so far as it would go, and afterwards replaced by the proceeds of bonds, overdrafts or notes of the company, which, to the extent necessary, were used to pay regular dividends. It is in this course of proceeding that counsel claims that defendant was clearly guilty of a violation of section 309 of the Civil Code irrespective of any difference of views as to what are and what

are not current expenses justly chargeable against the gross receipts of a mining corporation in order to determine its net or surplus earnings or profits." The court held that the directors of a mining corporation which has become indebted either by acquiring its property incumbered with debt, or by making permanent improvements for the thorough and systematic working of the mines and other property, would not be guilty of an infraction of section 309 of the Civil Code of California merely because they declared and paid dividends out of the net proceeds of the mine without paying the whole of such debts. It was further held that if the directors have fairly and honestly applied towards the payment and extinguishment of the debts of the company, a share of the net earnings satisfactory to its creditors and reasonably proportioned to the amount of its indebtedness, the extent and permanence of its mine, or the rate at which it is being exhausted, they may properly and safely pay out the remainder in dividends, because such remainders may in such cases be justly regarded and treated as surplus profits of the business.[1]

[1] Excelsior Water & Mining Co. *v.* Pierce, (1891) 90 Cal. 131. *Arguendo*, the court said: "The term 'capital stock' has a double meaning, as applied to corporations. In one sense it is the sum mentioned in the articles of incorporation as the amount of the capital stock; in other words, it is the share capital, or nominal capital, and does not necessarily represent a corresponding amount of actual capital. In case of mining corporations it is always arbitrary and generally extravagant in amount. The capital stock referred to in the statute, however, is the actual property of the corporation contributed by the shareholders of the nominal capital. In this case the nominal or share capital of the plaintiff was $5,000,000. Its actual capital was its mining and other property (less the debt with which it was incumbered) received in exchange for the shares which it issued, and this actual capital was what it was forbidden to divide. This inhibition, however, did not extend to the net proceeds of its mining operations, for a mining corporation, like any other corporation organized for the purpose of utilizing a wasting property, a property that can be used only by consuming it, as a mine, a lease or a patent, is not deemed to have divided its capital merely because it has distributed the net proceeds of its mining operations, although the necessary result is that so much has been subtracted from the substance of its estate. Moraw. on Corporations, § 442; Lee *v.* Neuchatel Asphalte Co., L. R., 41 Ch. Div. 24. It may distribute its net earnings, although the value of its mine is thereby diminished. But it may not sell the mine, or any part of it, and distribute the proceeds. In this sense, and in this sense only, provisions of law similar to those of section 309 of our Civil Code have been held to apply to mining corporations. If the mine belonging to a mining corporation when it commences operations is free from debt, and furnished with all necessary openings and appliances for its convenient

§ 389. **Borrowing money to pay dividends.**— As to the borrowing of money to pay dividends on the part of a mining corporation, the Supreme Court of California has said: "We think there are circumstances which do justify it. A mining company is working its mines at a profit, but discovers that they can be worked to better advantage by constructing a new tunnel; that is to say, it will be wise economy to incur an expense of, say a hundred thousand dollars to construct such a tunnel; that it will in fact add more than that sum to the value of the property. Clearly, we think, the corporation would be justified in incurring a debt to that amount to carry out the object, and that it could go on declaring dividends after providing for the payment of the accruing interest, and for the gradual extinction of the principal of such debt. But suppose, instead of borrowing in advance to meet payments on the tunnel, it makes some of the payments out of the current profits of its mining operations — profits justly applicable, at its option, to the payments of dividends, but not presently needed to meet a declared dividend. Afterwards, it borrows money, no more than it might have borrowed originally

working, the problem of ascertaining the amount of its surplus profits from time to time would be very simple, and would consist in merely deducting the gross outlay from the gross receipts, and the balance, less a reasonable reserve to meet contingencies, would be the legitimate subject of a dividend. But when the mining property has been taken subject to a debt, or when, as a preliminary operation, it becomes necessary to incur a debt in running an expensive tunnel or sinking an expensive shaft, the problem becomes complicated. Must the whole of such debts be paid out of the first earnings before making a dividend, or must only a part be paid? and if so, what part? We do not think it would be necessary to pay, in the first place, the whole of such debts, but it would be necessary to pay accruing interest, and to provide a sinking fund sufficient to extinguish the principal before the mine was exhausted. There can be no doubt, we think, that this is a correct theory; but in case of a property of such uncertain, fluctuating and precarious value as a mine, it would undoubtedly be extremely difficult in most cases to practically apply it. Fortunately, however, the rights of the creditors to insist upon payment of their demands as they fall due, and the prudence of capitalists to whom the company would be compelled to resort for loans with which to extend the payment of its maturing indebtedness, would always furnish a due corrective for any disposition of the directors of a corporation to provide an inadequate fund for the extinguishment of its indebtedness, and it may be safely assumed that in the case supposed, unless the debts of the corporation were paid at a rate satisfactory to its creditors, they would put a stop to the payment of dividends by the means within their power."

on account of the tunnel, and, out of the money so borrowed, replenishes the fund applicable to dividends. In such a case, the result is precisely the same as if the money had been borrowed sooner, and the identical money borrowed paid out on the tunnel. Nothing has been accomplished beyond what the directors had a right to do, and surely the mode in which it has been done can make no difference. In fact, the transaction may be regarded as a temporary borrowing from the dividend fund of a sum necessary to meet an immediate demand, with the advantage to the corporation of keeping its money employed and saving in the payment of interest." [1]

§ 390. **Rescinding a declaration of dividend.**— A late case before the Supreme Court of Judicature of Massachusetts, it having been reported to that court from a judgment of the trial court for their consideration, disclosed the following facts: That on a certain date a dividend of twenty per cent upon the capital stock of a manufacturing corporation was ordered to be paid on a day fixed. On the same date the annual meeting of stockholders occurred and a new board of directors was elected, two only of the old board being re-elected. The new board on the same day, by resolution, rescinded the resolution directing a dividend of twenty per cent and declared a dividend of six per cent payable on the day fixed. It also appeared that no money was set aside or provided to pay the dividend declared of twenty per cent, but the company had ample means and facilities for paying it; that always before this time money had been provided to pay a dividend before it was declared; that money to pay the six per cent dividend was provided after the meeting and before it was to be paid by borrowing, and it was set aside and deposited in bank for the purpose; that checks were sent to all the stockholders,

[1] Excelsior Water & Mining Co. *v.* Pierce, (1891) 90 Cal. 131, 143, 144. The court cited Union Pacific R. R. Co. *v.* United States, 99 U. S. 420; Park *v.* Grant Locomotive Works, 40 N. J. Eq. 113, and Minot *v.* Paine, 99 Mass. 101; s. c., 96 Am. Dec. 705, as authority for the proposition that the apportionment of net earnings to the payment of cash dividends, stock dividends, increase of capital, reserve or contingent fund, or to provide for future obligations, is largely one of policy, intrusted to the discretion of the directors, which, when honestly and intelligently exercised, will not be lightly overruled. See, also, Stringer's Case, L. R., 4 Ch. App. 490; Williams *v.* Western Union Tel. Co., 93 N. Y. 162; Zellerbach *v.* Allenberg, (1893) 99 Cal. 57; s. c., 33 Pac. Rep. 786.

including the plaintiff in this case, for this six per cent dividend by the treasurer of the company; that he declined to accept the check and returned it to the treasurer. The twenty per cent dividend had been paid to no stockholder, and a majority of stockholders had accepted the six per cent dividend. The plaintiff, after demanding the payment of the twenty per cent dividend, which was refused, brought this action upon contract for money had and received to recover the same from the corporation. The trial judge declined to rule as requested by the corporation, that the directors elected at the annual meeting of stockholders had a right on that day to rescind the vote whereby the twenty per cent dividend was declared payable at a future day, and that the plaintiff could not recover, and ordered judgment for the plaintiff. The Supreme Court reversed this judgment.[1]

[1] Ford *v.* Easthampton Rubber Thread Co., (1893) 158 Mass. 84. The reasoning of FIELD, Ch. J., speaking for the court in support of this judgment was as follows: "It seems to be settled that, when a dividend has been fully declared, the corporation thereby manifests its intention that the amount of the dividend should be considered as having been separated from the other property of the corporation, and as having become the individual property of the stockholders, and that, therefore, when the dividend becomes payable according to the terms of the vote declaring it, each stockholder has a right to demand payment of the proportional part of the dividend which belongs to his shares of stock, and to sue the corporation for it, if it is not paid on demand. In some cases money or other property equal to the whole amount of the dividend declared has been specifically set apart as a fund appropriated to the payment of the dividend, and the stockholders have been regarded as the *cestuis que trust* of this fund, each entitled to his share. In other cases the corporation has credited the stockholders with the amount of their shares of the dividend, and the stockholders have assented to this, and the amount so credited has been regarded as a debt of the corporation to the stockholders; or the corporation has paid to some of the stockholders their shares of the dividend, and has refused to pay anything to the others, and it has been held that the corporation must pay all alike. See Beers *v.* Bridgeport Spring Co., 42 Conn. 17; State *v.* Baltimore & Ohio Railroad, 6 Gill, 363; King *v.* Paterson & Hudson River Railroad, 5 Dutch. 504; Jermain *v.* Lake Shore & Michigan Southern Railway, 91 N. Y. 483; Hopper *v.* Sage, 112 N. Y. 530; Jackson *v.* Newark Plankroad Co., 2 Vroom, 277; Wheeler *v.* Northwestern Sleigh Co., 39 Fed. Rep. 347. When a dividend has been declared payable at a definite future time, but no fund has been set apart for the payment of the dividend, and the corporation meanwhile becomes insolvent, whether the stockholders to the extent of their proportions of the dividend should share ratably with the creditors of the corporation in its property has not, so far as we know,

§ 391. Contracts within and outside the power of private corporations.— It is not *ultra vires* a mining corporation to contract to advance a specified sum of money for the construction

been recently considered, but the decision in Lowene *v.* American Ins. Co., 6 Paige, 482, is that they should. The setting apart of a fund to pay a dividend has been held to give a lien upon it to the stockholders, which they can enforce to the exclusion of the general creditors of the corporation. In re LeBlanc, 14 Hun, 8, and 75 N. Y. 598; LeRoy *v.* Globe Ins. Co., 2 Edw. Ch. 657. The English Companies Act, 1862 (25 & 26 Vict. chap. 89, § 38, cl. 7), provides that 'no sum due to any member of a company, in his character of a member, by way of dividends, profits or otherwise shall be deemed to be a debt of the company, payable to such member in a case of competition between himself and any other creditor not being a member of the company; but any such sum may be taken into account, for the purposes of the final adjustment of the rights of the contributories amongst themselves.' Upon these questions, however, we desire to express no opinion. It has been argued that there is no consideration for the promise of a corporation to pay a dividend to its stockholders, but we think that the doctrine of consideration applicable to a simple contract between persons having no fiduciary relations to each other is not applicable to such promise. It is the object of a private business corporation to make money for its stockholders, and under our laws it is ordinarily the duty of the directors, from time to time, to declare dividends out of the net earnings, if there are any, and it must be left largely to the discretion of the directors to determine when and for how much such dividends should be declared. The whole property of the corporation is held on a sort of trust for the stockholders, and the directors are, in a general sense, the managers, and when a dividend is declared by the directors the declaration is a determination by a body authorized to make it that the amount of the dividend should be taken from the property of the corporation and paid over to the stockholders. The cause of action of each stockholder against the corporation for non-payment of the dividend does not arise from any actual contract between the corporation and its stockholders, but from the nature of the organization and the relation of the stockholders to the corporation and its property. Unless the rights of creditors intervene, or the corporation is enjoined from paying the dividend, on the ground that the dividend has not been earned, or on some other ground, the amount of the dividend, after it has been declared and has become payable, is considered as the property held by the corporation for the use of the stockholders individually, and the stockholders may recover their shares as money or property had and received to their use." Upon the point directly made here it was said: "We have been able to find little or no authority on the precise question involved in this case, namely, whether, after a dividend has been duly declared by a vote of the directors, but payable at a future time, the vote can be rescinded at a subsequent meeting of the directors, held before the time at which the dividend becomes payable according to the vote, when the fact that a dividend has been declared has not been made public or in any manner communicated to the stockholders, and when no fund has been set apart for the payment of the dividend. On principle, we do not see

of a tunnel to drain its mine, etc. Such a contract comes within the implied or incidental powers of such a corporation.[1] A contract between two corporations for consolidation, without express

why the directors may not rescind such a vote under the circumstances stated. By the vote no specific property passed to the stockholders. If the vote be regarded as a declaration of trust in favor of the stockholders it could be revoked before it was communicated to them or any property was identified or set aside for them. Indeed, cases may easily be supposed of such a change in the affairs of a corporation, between the time when a dividend is declared and the time when it becomes payable, to make the exercise of such a power by the directors useful, if not necessary, for the successful continuance of the business of the corporation. It appears in the present case that the meeting of the new directors at which the vote was rescinded was held after the annual meeting of the stockholders, but on the same day as the meeting of the directors at which the vote was passed, which was held just before the meeting of the stockholders, and that at the meeting of the stockholders 'the president did not, as had for many years been the custom, announce that any dividend had been declared or promulgate the same to the stockholders,' and it does not appear that any of the stockholders, except the directors, knew of the original vote, or that any of the stockholders had made any contracts, incurred any liability or done anything relying on the vote. It also appears that no fund was distinctly set apart for the payment of the dividend before the vote was rescinded. As the passage of the vote did not constitute an actual contract of the corporation with its stockholders, but was merely a mode of dividing the earnings of the property of the corporation among the stockholders, we are of opinion that before the division had been actually made, and before the position of the stockholders had been changed in reliance on the vote — certainly before the passage of the vote had been made public or communicated to the stockholders — it was within the power of the directors, at a meeting subsequent to that at which the vote was passed, to rescind it. In this action at law we cannot supervise the exercise of this power by the directors."

[1] Sutro Tunnel Co. *v.* Segregated Belcher Mining Co., (1885) 19 Nev. 121: s. c., 7 Pac. Rep. 271. HAWLEY, J., for the court, distinguished Davis *v.* Old Colony R. R. Co., 131 Mass. 258, and said: "It is apparent that the doctrines announced in that decision are not applicable to the facts of this case. There the benefits to the corporations were wholly disconnected, remote and foreign to the business in which they were engaged. Here the benefit to appellant is direct. The construction of the lateral tunnel, if not absolutely necessary, was certainly a convenient and appropriate means to drain its mine and enable it properly to conduct and carry on its legitimate business of mining in a systematic and scientific manner. In Brice's Treatise on the Doctrine of Ultra Vires it is said that 'Corporations may transact, in addition to their main undertaking, all such subordinate and connected matters as are, if not essential, at least very convenient to the due prosecution of the power,' and that, under many circumstances, 'they are in a manner necessitated to engage in business which is not within the mere letter of their constitution.' Green's Brice's

legislation authorizing it, would be *ultra vires*.[1] The Tennessee Supreme Court has held the guaranty of eight per cent dividend upon the stock of an elevator company, as an inducement to subscription to the capital stock of the latter, by a railroad corporation empowered by its charter "to do all lawful acts properly incident to a corporation and necessary and proper to the transaction of the business for which it was incorporated," with a declaration in its charter that it should "possess such additional power as may be convenient for the due and successful execution of the powers granted in their charter," was beyond its power.[2] In proceedings to condemn land for railroad purposes, where it appeared that one of the subscribers to the capital stock of the petitioning

Ultra Vires, 89. In applying these principles the courts have held that a corporation created for the purpose of mining and transportation of coal had the power to purchase and use a steamboat for the purpose of carrying its coal to market (Callaway M. & M. Co. *v.* Clark, 32 Mo. 305); that a corporation created for the purpose of raising and smelting lead ore had power to purchase smelting works and assume a a contract entered into by their vendors providing means for the transportation of their ores, when smelted, to market (Moss *v.* Averell, 10 N. Y. 455); that a corporation created for the purpose of carrying on an iron furnace is authorized to carry on a supply store in connection with that business (Scaright *v.* Payne, 6 Lea., [Tenn.] 283); that railroad corporations have the right to own and control steamboats for the purpose of transporting their freight and passengers across navigable waters on the line of their routes, and also at the end of their roads, separating them from the substantial *termini* of their routes (Wheeler *v.* San Francisco & A. R. Co., 31 Cal. 65); that where power is given to a railroad corporation to transport persons and property beyond the *termini* of its road, it has authority to purchase and use a steamboat for that purpose (Shawmut Bank *v.* Plattsburg & M. R. Co., 31 Vt. 496); that a railroad corporation, authorized to carry passengers and transport freight beyond its own lines, and to run steamboats for that purpose, may hire, either by the trip or by the season, steamboats belonging to others, or employ such steamboats to carry passengers and freight in connection with its own railroad and business, and guarantee to the proprietors that their gross earnings for the season shall not fall below a certain sum. Green Bay & M. R. Co. *v.* Union Steamboat Co., 107 U. S. 101. These and numerous other kindred cases proceed upon the theory that if the contract of the corporation is reasonably confined and connected with the business in which the corporation is engaged it comes within its implied or incidental powers. 'Corporations may so far develop and extend their operations as to engage in matters not primarily contemplated by their founders, provided these matters come fairly within their scope, and provided, also, that in so developing and extending their undertaking they employ direct and not indirect means.' Green's Brice's Ultra Vires, 90."

[1] Home Friendly Society *v.* Tyler, (1890) 9 Pa. Co. Ct. Rep. 617.

[2] Memphis Grain & Elevator Co. *v.* Memphis & Charleston R. R. Co., (1887, Tenn.) 5 S. W. Rep. 52.

corporation was a corporation, and that its subscription was essential to make up the required amount, the New York Court of Appeals held that, in the absence of any proof, it would not be presumed against the act of the corporation, and its payment of the percentage required that it acted beyond its powers.[1] Whether or not the purchase of real property in another state by a Vermont corporation was within its corporate powers, the Supreme Court of that state held it should account for the actual value of what it received.[2] Lending money by a trading corporation to one dealing with it to enable him to carry on the transactions is not *ultra vires* on the part of the corporation.[3]

§ 392. **Rules as to estoppel to plead that contracts are ultra vires.**— A corporation giving its note for the price of stock of another corporation cannot defend in a suit upon it on the ground that the corporation taking the note had no right to

[1] In the Matter of, etc., Rochester, Hornellsville & Lackawanna R. R. Co., (1888) 110 N. Y. 119; s. c., 17 N. E. Rep. 678.

[2] Moore *v.* Swanton Tanning Co., (1888) 60 Vt. 459; s. c., 15 Atl. Rep. 114. In Mallory *v.* Hanaur Oil Works, (1888) 2 Pickle, (Tenn.) 598; s. c., 8 S. W. Rep. 396, an agreement between two corporations engaged in manufacturing the same article, to select a committee composed of representatives of each corporation, and to turn over to this committee the properties and machinery of each corporation, to be managed and operated for the common benefit — the profits and losses to be shared in agreed proportions — was held to be but a contract of partnership, and that the contract was not within the express or implied powers of corporations organized under the Tennessee Incorporation Act of 1875 (Chap. 142), and was *ultra vires* and void so far as it was unexecuted, even though authorized by both shareholders and directors. This contract was entered into for three years; two years had expired. The court held it unexecuted as to the three years in the sense that it might be repudiated as *ultra vires*, and the property delivered at once recovered by the corporations, citing as authority Thomas *v.* Railroad Co., 101 U. S. 71. For a transaction on the part of a corporation which was held not to be within the prohibition of the Code of West Virginia forbidding one corporation to subscribe for or purchase stocks, bonds or securities of another, see County Court of Taylor County *v.* Baltimore & Ohio R. R. Co., (1888) 35 Fed. Rep. 161. When a corporation for brewing cannot become a surety, see Filon *v.* Miller Brewing Co., (1891) 60 Hun, 582; s. c., 15 N. Y. Supp. 57.

[3] Holmes, Booth & Haydens *v.* Willard, (1891) 53 Hun, 629; s. c., 5 N. Y. Supp. 610; affirmed in 125 N. Y. 75; s. c., 25 N. E. Rep. 1083. Illustrations of an *ultra vires* contract: Simmons *v.* Troy Iron Works, (1891) 92 Ala. 427; s. c., 9 So. Rep. 160; Shaw *v.* Campbell Turnpike Road Co., (1891, Ky.) 15 S. W. Rep. 245; Tennessee River Transportation Co. *v.* Kavanaugh (1891) 93 Ala. 324; s. c., 9 So. Rep. 395. Illustration of when a contract is executory and the defense of *ultra vires* may be made: Bowman Dairy Co. *v.* Mooney, 41 Mo. App. 665.

acquire title to the stock.[1] The receipt of goods purchased for a business outside of that authorized by the charter of a corporation will not estop the corporation from the defense that it was *ultra vires* in an action to recover the price.[2] In a case before the Court of Errors and Appeals of New Jersey it appeared that a

[1] Holmes & Griggs Manufacturing Co. *v.* Holmes & Wessell Metal Co., (1889) 53 Hun, 52; s. c., 5 N. Y. Supp. 937; affirmed in 127 N. Y. 252; s. c., 27 N. E. Rep. 831.

[2] Chewacla Lime Works *v.* Dismukes, (1889) 87 Ala. 344; s. c., 6 So. Rep. 122. As to estoppel of corporation by reception of benefits to complain of a contract as *ultra vires*, see Sherman Center Town Co. *v.* Morris, (1890) 43 Kans. 282; s. c., 23 Pac. Rep. 569; Sherman Center Town Co. *v.* Russell, (1891) 46 Kans. 382; s. c., 26 Pac. Rep. 715; Cunningham *v.* Massena Springs & Ft. C. R. Co., (1892) 63 Hun, 439; s. c., 18 N. Y. Supp. 600; Rio Grande Cattle Co. *v.* Burns, (1892) 82 Tex. 50; s. c., 17 S. W. Rep. 1043; McNab *v.* McNab & Harlin Manufg. Co., 62 Hun, 18; s. c., 16 N. Y. Supp. 448; Dewey *v.* Toledo, A. A. & N. M. Ry. Co., (1891) 91 Mich. 351; s. c., 51 N. W. Rep. 1063; Campbell *v.* Argenta Gold & Silver Mining Co., (1891) 51 Fed. Rep. 1; Bond *v.* Terrell Cotton & Woolen Manufg. Co., (1891) 82 Tex. 309; s. c., 18 S. W. Rep. 691. Estoppel to plead *ultra vires:* Manchester & L. Railroad *v.* Concord Railroad, (N. H. 1891) 20 Atl. Rep. 383; Witter *v.* Grand Rapids Flouring Mill Co., (1891) 78 Wis. 543; s. c., 47 N. W. Rep. 729; Sherman Center Town Co. *v.* Fletcher (1891) 46 Kans. 524; s. c., 26 Pac. Rep. 951; Heims Brewing Co. *v.* Flannery, (1891) 137 Ill. 309; s. c., 27 N. E. Rep. 286; First Nat. Bank *v.* Strang, (Ill. 1891) 27 N. E. Rep. 903; Columbia Electric Co. *v.* Dixon, (1891) 46 Minn. 463; s. c., 49 N. W. Rep. 244. When a secured creditor cannot object that a mortgage for a sum in excess of the indebtedness allowed by the charter of a corporation was *ultra vires* and invalid: Allis *v.* Jones, (1890) 45 Fed. Rep. 148. When a corporation cannot object that a purchase of a certain franchise by it was *ultra vires:* Starin *v.* Edson, (1889) 112 N. Y. 206; s. c., 19 N. E. Rep. 670. Objection that a contract was *ultra vires* open only to the state or a stockholder: Baker *v.* Northwestern Guaranty Loan Co., (1883) 36 Minn. 185; s. c., 30 N. W. Rep. 464. As to the rule that municipal corporations are not estopped to deny the validity of contracts *ultra vires* made by their officers, see Newbery *v.* Fox, (1887) 37 Minn. 141; s. c. 33 N. W. Rep. 333; Mayor *v.* Ray, 19 Wall. 468; Brady *v.* Mayor, etc., of New York, 20 N. Y. 312; Hague *v.* City of Philadelphia, 48 Pa. St. 527; Nash *v.* City of St. Paul, 8 Minn. 172. That contracts *ultra vires* on the part of a municipal corporation cannot be legalized by any action on its part in the way of acknowledgment, ratification or otherwise, see Lyddy *v.* Long Island City, (1887) 104 N. Y. 218; s. c., 10 N. E. Rep. 155. As to enjoining in behalf of stockholders, as *ultra vires*, the purchase of another railroad by a railroad corporation, see Mackintosh *v.* Flint & Pere Marquette R. R. Co., (1888) 34 Fed. Rep. 582. Estoppel of stockholders to complain that debt incurred was in excess of the limit of indebtedness fixed in charter: Poole *v.* West Point Butter & Cheese Assn., (1887) 30 Fed. Rep. 513. That one who has received the benefits of a contract is not in position to raise the question that the contract on the part of the corporation was *ultra vires*, see Dia-

railroad corporation had entered into a contract with another that the latter would build a line of railroad which was authorized by its charter; that the former would guarantee the bonds of the latter to cover the cost of construction of the road, and would take a lease for 999 years of the road from the latter, for which it would pay so much rental per annum; that the road was built, the bonds guaranteed, the lessee went into possession of the road under the lease, complied with its terms for nine years, and then sought to repudiate the contract as one which was *ultra vires* on its part. The court held that under the statement of facts it was an executed contract, and that the corporation must be held to the performance of its part of the contract, the other having performed its side of the same, and the plea of *ultra vires* was not available for avoiding a specific performance.[1]

mond Match Co. *v.* Roeber, (1887) 106 N. Y. 473; s. c., 13 N. E. Rep. 419. When one contracting with a corporation cannot set up as a defense to a suit upon such contract that it was *ultra vires* on the part of the corporation, see Slater Woolen Co. *v.* Lamb, (1887) 143 Mass. 420; s. c., 9 N. E. Rep. 823. Estoppel of one receiving benefits to plead lack of power on the part of the corporation: Watts-Campbell Co. *v.* Yuengling, (1889) 51 Hun, 302; s. c., 3 N. Y. Supp. 869.

[1] Camden & Atlantic R. R. Co. *v.* May's Landing & Egg Harbor City R. R. Co., (1886) 48 N. J. Law, 530; s. c., 7 Atl. Rep. 523. VAN SYCKEL, J., speaking for the court, after referring to the numerous cases, English and American, touching this question, said: "In the conflict of judicial decision on this subject, this court may adopt and should adopt the rule which will produce the best results in the administration of justice. In my judgment the true rule is that when the transaction is complete, and the party seeking relief has performed on his part, the plea of *ultra vires* by the corporation which has acquiesced in it, is inadmissible in an action brought against it for not performing its side of the contract in all those instances where the party who has performed cannot, upon rescission, be restored to his former status. In the cases maintaining the contrary doctrine the reasoning of the courts has been: 1. That corporators might, by ratifying corporate acts, by their acquiesence, infinitely extend and amplify their granted powers. 2. That consent on the part of those who do an act which they have no power to do cannot make it legal. 3. That to hold that an act performed in executing a void contract makes all its parts valid, is to say that the more that is done under an unauthorized contract, the stronger is the claim to its enforcement by the courts. To the first objection a sufficient answer is that the state may interpose its authority at any time, and compel an abandonment of the act in excess of power, and, if need be, revoke the charter of the company for its usurpation. When the state challenges the legality of the transaction, the paramount and only question is whether it has bestowed upon the company the requisite authority to engage in it. When the question arises between the company and the other party to the contract, other legal principles apply in determining whether the contract shall be ob-

served. It will be admitted that where there is an absence of authority on the part of a corporation to do an act the requisite power cannot be imported into the transaction, either by the consent of stockholders or by the execution of the contract by the other party to the agreement. The contract must necessarily continue to be *ultra vires*. No such effect has been attributed in any of the cases to acquiescence or unilateral performance. The basis upon which the enforcement of the contract in such cases rests is that the company is estopped from setting up its own unauthorized act, and its own incapacity to evade performance on its part, after receiving the fruits of the bargain. The power of the company is not amplified, the agreement is none the more legal, in the sense that there was authority to execute it; the court simply refuses to entertain the defense which common honesty forbids the company to make. A man may become bound by the act of an unauthorized agent, and be held liable to the contract made for him, not on the ground that the agent in fact had any authority, but for some conduct on the part of the alleged principal which precludes him from raising the question of authority. No reason is perceived why the rules of fair dealing, which are so rigorously applied to natural persons, shall not pertain as strictly to private corporations. No instance is known where a natural person can set up in his own behalf, and for his own advantage, his want of authority to do an act for which he has received the consideration from the other party. Transactions which are immoral, illegal, forbidden by statute or contrary to public policy, are not embraced in this discussion; they cannot furnish the basis for a legal cause of action. Why is it that *ultra vires* contracts are recognized as unassailable, and are permitted to stand as the foundation of rights acquired under them after they have been executed on both sides? Such execution imparts no additional powers to the corporate body. It does not transmute the negative into the positive. The absence of power is as apparent after as before performance. Why is it that corporations are compelled to pay money borrowed in excess of authority, and to pay the stipulated rent for premises unlawfully leased for the period of occupation? The law does not imply a contract to pay the bondholders the money they received. It is illogical to say that the law will imply a contract by the company which it has no power to make for itself. A contract cannot be implied where an express contract cannot be made. The law recognizes the obligation; it precludes or estops the attempt to evade it. Apply to it what legal phrase you may, the underlying principle is that the corporation cannot set up its own infirmity when it is unconscionable to do so. The law forbids the defense on account of the flagrant injustice which would otherwise be done. The question of corporate power is not entertained. To enable recompense to be had to this extent the contracts are respected, not that they rest in authority, but because good conscience requires it. * * * But acquiescence in it, upon which the other party acts, may, and does, upon settled legal principles, preclude the parties from starting the question of power as between themselves. There is, in fact, a subsisting contract, actually executed in due and legal form, which, under the rule stated, is unimpeachable, except at the instance of the state. It is thus, in legal contemplation, impressed with the vigor and incidents of a valid contract as between the parties, and there is no difficulty in enforcing it in a suit of law."

As to "Fiscal Management — Private Corporations," see further, chapter 4, "Power of Agents and Officers — Private Corporations."

CHAPTER XVIII.

COUNTY BONDS.

§ 393. County bonds generally.
394. Bonds issued for refunding indebtedness.
395. Bonds not within the power of a Texas county to issue for the erection of court houses.
396. Rights of holders of such bonds.
397. The effect of a statute of Texas as to county bonds in which school funds may be invested.
398. Validity of bonds as affected by the place of execution.
399. Validity of bonds as affected by constitutional requirements.
400. Validity of bonds as affected by limitations as to indebtedness.
401. The validity of judgments against a county for which the bonds were issued cannot be questioned in actions on the bonds.
§ 402. The statements of a county's agent in sale of the bonds not operative as an estoppel upon the county to refund.
403. When a county may plead an overissue.
404. When the defense that a county was not fully organized when the bonds were issued is not open to the courts.
405. Counties suable in federal courts.
406. Plea of Statute of Limitations on county bonds.
407. When statute as to presentation of claims is not applicable to judgments upon bonds and coupons.
408. The proper proceeding of courts where some of the bonds of a series are valid and others invalid.

§ 393. **County bonds generally.**— The power of counties to issue bonds is not inherent or general.[1] When municipal bonds are found in circulation, it will be presumed that the legal steps have been taken to authorize their issue.[2] Bonds issued by county commissioners for the purpose of constructing public buildings must bear interest payable annually. If bonds were issued for interest, payable in a shorter period, the Indiana Supreme Court held their issuance might be enjoined. The statute authorizing them should be strictly complied with.[3] Municipal bonds are a class of negotiable paper.[4] The Illinois Supreme Court has held as to these bonds that their negotiable character would not protect the purchaser, before maturity, against the consequences

[1] Thayer *v.* Montgomery County, 3 Dill. 389. As to the power to issue bonds, see Supervisors of Schuyler County *v.* Farwell, 25 Ill. 181.

[2] Maxcy *v.* Williamson County, 72 Ill. 207.

[3] English *v.* Smock, 34 Ind. 115.

[4] Callanan *v.* Brown, 31 Iowa, 333; Griffith *v.* Burden, 35 Iowa, 138.

of a want of authority to issue them; also, that the bonds having been issued without authority and, therefore, void, the mere levy of taxes and payment of interest on them by the county did not render them valid.[1] A county will not be deprived, by its bonds having passed by assignment into the hands of *bona fide* holders, of any defense which it would have against parties to whom the bonds were issued.[2] A municipal corporation will not be bound

[1] Supervisors of Marshall County *v.* Cook, (1865) 38 Ill. 44. The court distinguished certain cases relied upon as contrary to its views in these words: "In the case of Mercer County *v.* Hackett, 1 Wall. 83, it was held that slight and immaterial omissions in ordering the bonds to issue will not render them invalid in the hands of an innocent holder. In that case the recommendation was by the grand jury, the body authorized by law to make it, but they did not make it in the precise language of the law, but it was substantially good. If the recommendations had been made by the petit jury it would have presented a very different question and one more like the one under consideration than the one discussed in that case. We do not see that the court could have done otherwise than decide as they did. It was not a question of power to act, but whether the action, defective though it might be, was still in pursuance of the power. It is supposed that the case of Gelpcke *v.* City of Dubuque, 1 Wall. 175, is in conflict with the views here expressed. It will be observed, however, that so far as the record discloses in that case, the law authorizing the bonds to issue had been strictly observed in every particular before they were issued. A curative act had been passed by the legislature declaring the bonds valid and binding. That case does not, like the present, depend upon the power of the body issuing them to act, but upon other and different questions, the principal one of which was the constitutionality of the law. Hence, that case and this differ essentially in the questions presented and discussed. It is true the court use broad and comprehensive language. They say: 'When a corporation has the power, under any circumstances, to issue negotiable securities, the *bona fide* holder has a right to presume they were issued under the circumstances which gave the requisite authority, and they are no more liable to be impeached for any infirmity in the hands of such holder than any other commercial paper. If there were any irregularity in taking the votes of the electors, or otherwise, in issuing the bonds, it is remedied by the curative provisions of the act of January 28, 1857.' The court, however, do not intimate that such instruments, issued without power, would be protected in the hands of any kind of a holder. The court proceed upon the ground that the persons issuing the bonds did so in the exercise of a power. And that if there was a defective exercise of the power, the irregularity had been cured by the act of the legislature. There is no intimation that bonds void in their inception — issued in direct violation of law — would be protected. Nor do we believe that court will so hold if this question should ever be presented for their determination."

[2] Board of Commissioners of Madison County *v.* Brown, 28 Ind. 161. In Melvin *v.* Lisenby, 72 Ill. 63, the county was authorized to issue bonds by a law providing that the bonds should be executed by certain officers, and countersigned by the county treasurer of the

by an issue of bonds in excess of the constitutional limit of municipal indebtedness; neither will it be liable to pay back what has been received thereon.[1] In case bonds purport to have been issued by virtue of a certain order, named and referred to, but not copied or described, those claiming any rights by virtue of such bonds are chargeable with notice of the contents of the order.[2] Where there are recitals in county bonds that they were issued in accordance with the statute and authorized by a vote of the people made by officers invested by the statute with the power of deciding whether these conditions have been fulfilled or not, the bonds will not be open to the defense of want of consideration or of fraud on the part of the officers, or of non-compliance with the conditions precedent to the right to exercise the power.[3] To provide a site for a state institution was held by the Illinois Supreme Court not to be a corporate purpose, and bonds issued by a county for such a purpose were held to be void; and that no matter in whose hands such bonds might be, where a tax had been levied and collected for their payment, or for the payment of the accrued interest upon them, the county treasurer might be restrained from applying the money collected for the payment of the bonds or interest.[4] Bonds issued by a county in payment of a judgment, under authority of statute, have been held in Iowa to be valid in the hands of a purchaser in good faith, for value, without notice of any claim that they were illegal for any cause, although the indebtedness for which the judgment was rendered was in excess of the constitutional limit of indebtedness, such defense not having been interposed in the suit by the board of supervisors of the county.[5] It is now well settled that where bonds of a county or municipality have been issued under authority of law, and where, at the same time, the law has directed

county. The court held the omission of the county treasurer to countersign the bonds to be a mere defect in the execution of them which a court of equity would, in the absence of a remedy at law, ordinarily supply, and that an injunction restraining the collection of taxes for the payment of the bonds issued should not be allowed.

[1] McPherson *v.* Foster, 43 Iowa, 48.

[2] Lewis *v.* Bourbon County, 12 Kans. 186.

[3] Carpenter *v.* Buena Vista County, 5 Dill. 556. The principle that the recital upon the face of bonds made a part of the bonds, must show that they were issued for some authorized purpose or object, applied in Thayer *v.* Montgomery County, 3 Dill. 389.

[4] Board of Supervisors of Livingston County *v.* Weider, (1872) 64 Ill. 427.

[5] Sioux City & St. Paul R. R. Co. *v.* Osceola County, 45 Iowa, 168; s. c., again in 52 Iowa, 26.

a tax to be levied for their protection, or where there is a general law authorizing and directing a tax in all like cases, applicable to said bonds, the law becomes a part of the contract. The holder is entitled to look to the taxing provisions as a part of his security, and has a vested right to demand, at the proper time, that it shall be exercised in his favor. The measure of that right will be the constitutional limit of the power which the legislature could grant to the municipality when the contract was made. Such contracts are protected by the Constitution of the United States, and no subsequent act of a state legislature or a constitutional convention can impair them.[1]

§ 394. **Bonds issued for refunding indebtedness.**— It appeared in a case before the United States Circuit Court of Appeals, an action upon refunding bonds of a county in Michigan, that suits had been brought upon the bonds originally issued, the holders had judgments against the county for the amounts due; that an act of the legislature was passed authorizing the county authorities to refund the county's indebtedness; that the county authorities did so, issuing the bonds which were the base of this action and giving them in exchange for the original bonds and judgments which constituted the indebtedness, the refunding of which the act authorized. The court held that, under the circumstances of this case, the bonds issued to refund the supposed indebtedness of the county were binding obligations upon the county.[2]

[1] Brodie *v.* McCabe, Collector, (1878) 33 Ark. 690.

[2] Ashley *v.* Board of Supervisors of Presque Isle County, (1893) 60 Fed. Rep. 55. The court said: "The former bonds were more than colorable obligations. Recoveries had been had in the United States Circuit Court against the reorganized county upon some of them, and the validity of the remaining ones was, to say the least, a fair question for controversy. The county chose not to make further defense to the bonds, and to avail itself of the opportunity to defer the payment of the indebtedness and to obtain a reduction of the interest from ten to seven per cent. It sought and obtained from the legislature authority to refund its debt. It procured the surrender of the former bonds and issued in their stead and in consideration of them, the new bonds. If the legislature did not assume the former bonds to be valid, it devolved upon the board of supervisors of the county to determine what were valid obligations of the county in exercising the authority to issue the new bonds conferred by the act, and such determination would bind the county. In the case of The City of Cadillac *v.* Woonsocket Institution, 58 Fed. Rep. 935, bonds had been issued under the guise of a law authorizing

§ 395. **Bonds not within the power of a Texas county to issue for the erection of court houses.**— Bonds issued by a county in Texas for the construction of a building intended primarily for a jail, to which use it was to be permanently devoted, though it was the purpose of the county commissioners to use it also as a court house until a court house could be built, the Supreme Court of that state held were not authorized by the laws of that state providing for the erection of court houses.[1]

public improvements for the actual purpose of aiding a railroad company. The bonds were in the hands of one who knew of the fraudulent evasion of the Constitution of the state, and no action could have been maintained upon them by him. But they were negotiable, and might have been put upon the market by him. In this state of affairs, the common council of the city, upon the request of a large number of its citizens, and upon considerations deemed by the council to justify it, issued new bonds to take up the former ones, under the provisions of the Michigan statute for refunding municipal indebtedness. The new bonds were exchanged for the old, and passed into the hands of *bona fide* holders, who brought suit upon them. One question involved in the case was, whether a buyer of the bonds — which on their face were refunding bonds — was bound to go back of the issue of the new bonds, which were regular on their face and contained recitals that they were issued in conformity with law, and ascertain the nature of the refunded indebtedness. The refunding statute did not, in terms, declare who should determine the fact of previous indebtedness. But, Judge LURTON, in delivering the opinion of the court, said: 'Power was conferred upon the common council to issue new bonds to take up old ones falling due. The question as to whether there were any such bonds is referred to the council. The old bonds, as the facts found, were at least colorable obligations. The council determined to issue new bonds to take them up. It seems to me that, under the circumstances, it did not devolve upon the purchaser of the new bonds to look into the validity of the funded old bonds.' Citing Coloma *v.* Eaves, 92 U. S. 484; Hackett *v.* Ottawa, 99 U. S. 86, and Chaffee Co. *v.* Potter, 142 U. S. 355; s. c., 12 Sup. Ct. Rep. 216. In the present case, the force of these suggestions is augmented by the fact that, by express provision of the Constitution of Michigan, boards of supervisors are empowered to adjust all claims against their respective counties, and from their decision there is no appeal. This jurisdiction is not exclusive, but, as against the county, any one having demands against it could obtain from the board a conclusive determination upon them. To require the purchaser of refunding bonds to scrutinize the sucessive issues in which the debt has been refunded to its root, would seriously impair the market value of the bonds, or otherwise work injuriously to the interests of the municipality issuing them."

[1] Nolan County *v.* The State, (1891) 83 Tex. 182. As to the power of counties in such cases, it was said: "It may be considered settled law in this state that one of its counties cannot issue bonds without an act of the legislature conferring that power. Robertson *v.* Breedlove, 61 Tex. 316. The case cited is also authority for holding that the act by virtue of which the bonds in question were issued, conferred

§ 396. **Rights of holders of such bonds.**—The Texas Supreme Court considered the question of the rights of the holder of certain county bonds issued by a county under the statute of that state authorizing the issuance of bonds for the erection of court houses, which bonds the court held were issued without authority, with the result of this declaration of the law controlling in this case: "[These] bonds are payable to bearer and in all other respects they are regular upon their face. They recite that they were issued for the purpose of erecting a court house for [defendant] county, and in pursuance of the authority conferred by the act of February 11, 1881. They also purport to have been registered by the treasurer of the county. The state is admitted to be a holder for value of the four bonds of this series which are in part the foundation of this suit; and it is also admitted that at the time of their purchase its agents had no actual notice of any fact which impaired their validity. The county [defendant] had no court house, and, therefore, the Commissioners' Court had power to issue bonds for the erection of such a structure containing all the recitals necessary to show the authority for the creation of the debt. If a purchaser were bound to inquire into the existence of the facts which empowered the court to issue bonds to build a court house, and to know that the county had no court house, in view of the recitals upon the face of the obligations he was bound to look no further. He had the right to rely upon the truth of such recitals, and having paid value for the bonds without actual knowledge of their ille-

authority to issue bonds upon such counties only as had no court house at their county seat. We think it equally clear that the only purpose for which the power could be exercised was to provide the means for building a court house. The act of February 2, 1884, which authorizes the issue of bonds for the construction not only of court houses but also of jails, tends to show that such is the legislative construction of the act under consideration. * * * Therefore, at the threshold of the discussion we are met with the question whether there was any authority whatever for the issue of the first series of bonds. It is not to be supposed that the legislature intended to confer the power upon the counties to create a bonded indebtedness to build a temporary structure to be used as a court house until a permanent building could be constructed. The limitations in the Constitution upon the creation of municipal debts, and the great caution manifested in conferring power upon municipal corporations to issue bonds, repel the idea that it could have been the purpose to authorize counties to issue them for the purpose of building other than permanent court houses."

gality, the county would be estopped to set up that they were not issued for the purpose for which they purported to be issued."[1]

§ 397. **The effect of a statute of Texas as to county bonds in which school funds may be invested.**— The state of Texas, having invested certain school funds in some of the bonds issued by the county in this case, was held to be protected by the statutes of Texas, which provided that: "In all cases where the proceeds of the sale of any bonds have been received by the proper officers of the county, or by a party acting for it in negotiating the sale thereof, such county shall be thereafter estopped from denying the validity of such bonds so issued, and the same shall be held to be valid and binding obligations of the county, and in any action upon such bonds or coupons thereto, judgment shall be rendered against the county for the amount of the bonds sued on and interest thereon at the rate mentioned therein, deducting such amounts, if any, as have been previously paid thereon." "The payment of any interest upon any bond heretofore purchased, or that may hereafter be purchased, with public school funds, or belonging thereto, shall be deemed and held a waiver of any supposed error, irregularity, or want of authority affecting or tending to affect the validity of any such bonds; and the same shall thereafter be held valid and binding obligations upon the county by which they appear or purport to have been issued, notwithstanding such supposed error, irregularity or want of authority as aforesaid." The court held the statutes to be constitutional, and also held adversely to the contention on behalf of the county that the statutes applied only to such bonds as may have been purchased by the state directly from the counties.[2]

[1] Nolan County *v.* The State, (1891) 83 Tex. 182, 194, 195, holding the bonds valid in the hands of the holder, unless the entire issue of the bonds was in excess of the amount of the indebtedness which the county was authorized by law to create. The Texas court recognized as authority for their ruling the following cases, to wit: Chambers County *v.* Clews, 21 Wall. 321; Wilson *v.* Salamanca, 99 U. S. 504; Marcy *v.* Oswego, 92 U. S. 640; Humboldt *v.* Long, 92 U. S. 644; Daviess County *v.* Huidekoper, 98 U. S. 100.

[2] Nolan County *v.* The State, (1891) 83 Tex. 182. It was said by the court: "That the provisions in question are not repugnant to the Constitution in the particulars urged against them, we think too well settled to require discussion. Ritchie *v.* Franklin County, 22 Wall. 74; New Orleans *v.* Clark, 95 U. S. 644; Cooley Const. Lim. (4th ed.) 466, 467. It can hardly be deemed an open question in this court. Morris

§ 398. Validity of bonds as affected by the place of execution.—A contractor for the erection of a court house in a county of Iowa having completed his contract, the county judge of the county delivered to him county bonds in payment. It would seem that these bonds proved not so negotiable as the contractor desired, and afterwards the county judge went to New York with the contractor and there made and issued to him new bonds for the same amount, differing in the amount of each, in time of payment, and in amount of coupons, and in other particulars; and he had a seal made there which he called the seal of the county, and affixed the seal to them and then delivered them to the contractor. The bonds were payable to the contractor or bearer. They were afterward sold to a third person, and upon his death his son brought action against the county upon them. The Code of Iowa at the time authorized the county judge, sitting as a County Court, to provide for the erection and reparation of court houses, jails and other necessary buildings within and for the use of the county. The question as to construction of the court house, levy of the special tax for the purpose, etc., was properly submitted to the voters of the county as required by the Code; a majority of the voters favored the proposition. The United States Supreme Court held that the issue of the bonds was authorized; that the county judge was clothed with the duty of deciding upon the question, and his decision, in the absence of fraud or collusion, was final, and neither party could go behind

v. The State, 62 Tex. 741; Blum *v.* Looney, 69 Tex. 3. Where a contract which a municipal corporation has attempted to create is invalid merely for want of legislative authority to create it, it can be made valid by a subsequent law. But if at the time of its attempted creation the legislature could not have authorized it, it may be doubted whether the legislature could make it valid, although in the meantime, by a change in the Constitution, the restriction upon its own power may have been removed. * * * There is nothing in the language of the validating act which indicates that it was not to be applied to bonds which may have been bought by the state after they had been transferred by the county to third parties. The object of the provision was to protect the school fund, and we see no reason why it was not intended to validate any county bond held by the state for the benefit of its public schools, whether purchased directly from the county or from intermediate holders." For a case holding bonds issued by a county for the erection of a court house and jail to be valid by force of an act of the legislature having the effect to make them valid by a subsequent grant of power to the county, and how far a *bona fide* purchaser without notice of any defect is protected, see Ball *v.* Presidio County, (Tex. Civ. App. 1894) 27 S. W. Rep. 702.

it.[1] They further held that it was no valid objection that the bonds were made payable and were sold beyond the limits of the county and of the state; that the power to issue them carried with it authority to the county judge as to both these things—to do what he deemed best for the interests of the county for which he was acting.[2]

§ 399. **Validity of bonds as affected by constitutional requirements.**—County records, when pointed to by the laws or constitutional provisions relating to the issuance of county bonds as evidence of facts required to authorize their issuance, and not the recitals in the bonds, must be looked to by all persons purposing to deal in the bonds. So, in this case, county bonds were held invalid, even in the hands of *bona fide* purchasers, they having been issued without compliance with the constitutional requirements that provision should be made at the time of incurring any debt for levying a sufficient tax to create a sinking fund of two per cent, in addition to meeting the interest.[3]

[1] Lynde *v.* The County, (1872) 16 Wall. 6. Mr. Justice SWAYNE, speaking for the court, referred to the rulings in Iowa on this subject in these words: "In Iowa every county is a body corporate. In Clapp *v.* The County of Cedar, 5 Iowa, 15, it was said by the Supreme Court of the state that the office of county judge being created and his powers and duties defined by statute, the principles of the law of agency where those powers and duties are drawn in question, have no application; that 'he is the living representative and embodiment of the county,' and that 'his acts are the acts of the corporation.' In Hull & Argalls *v.* The County of Marshall, 12 Iowa, 142, it was held that by virtue of his general authority he might contract for the building of a court house to be paid for out of the revenue of the county, but that when a debt was to be incurred for that purpose special authority must be conferred by a popular vote in the manner provided by the statute. It was further held that where a loan was thus authorized, the form of the securities not being prescribed, negotiable bonds might be issued. The statute provides that the judge may submit to the people, at a regular or special election, 'the question whether money may be borrowed to aid in the erection of public buildings,' and other questions not necessary to be mentioned; and that 'when the question so submitted involves the borrowing or expenditure of money,' it 'must be accompanied by a provision to levy a tax for the payment thereof,' and that 'no vote adopting the question proposed will be of effect unless it adopt the tax also.'"

[2] Lynde *v.* The County, (1872) 16 Wall. 6.

[3] Quaker City National Bank *v.* Nolan County, (1894) 59 Fed. Rep. 660; citing Citizens' Bank *v.* City of Terrell, 78 Tex. 456; s. c., 14 S. W. Rep. 1003; Dixon County *v.* Field, 111 U. S. 84; s. c., 4 Sup. Ct. Rep. 315; Lake Co. *v.* Graham, 130 U. S. 682

§ 400. Validity of bonds as affected by limitations as to indebtedness.—The effect of the constitutional provision of Texas, which it had been held limited the amount of indebtedness which counties, towns and cities were authorized to create for the erection of public buildings, etc., to twenty-five cents upon $100 worth of property as shown by the assessment rolls of the municipality,[1] was considered by the Supreme Court in connection with the other questions involved with reference to the county bonds for the erection of a court house issued in a case before that court.[2] The court had also held in a previous case that the word "valuation," as used in the constitutional provision, meant the value as fixed by competent authority for the purposes of taxation.[3] The result of the decisions in the case last cited, the court in this case stated to be that the governing boards of municipal corporations in that state are not empowered, when ascertaining the amount of an indebtedness to be created, to determine for themselves the aggregate value of the property therein subject to taxation, but are to be governed by the official rolls made out by the tax assessor. The power being limited as to the amount of the official assessment, it was held that the commissioners were not authorized to look beyond it and to determine the extent of their power from other data within their reach.[4] The court held that as to the excess of these bonds, over

s. c., 9 Sup. Ct. Rep. 654; Nolan Co. *v.* State, 83 Tex. 183; s. c., 17 S. W. Rep. 823; Francis *v.* Howard Co., 54 Fed. Rep. 487; s. c., 50 Fed. Rep. 60; 4 C. C. A. 460. It was held further that the legislature of Texas had no power to validate county bonds issued in violation of constitutional provisions which were alive and in force at the date of the validating act. Further, that a decision of the Supreme Court of that state, sustaining the statute which validated certain county bonds, was not controlling on the federal court, where it appeared that the bonds were void for failure to comply with a provision of the State Constitution, but that this point was not called to the attention of the state court, and its decision was based on other grounds.

[1] See Citizens' Bank *v.* Terrell, 78 Tex. 450.

[2] Nolan County *v.* The State of Texas, (1891) 83 Tex. 182.

[3] Citizens' Bank *v.* Terrell, 78 Tex. 450.

[4] Nolan County *v.* The State of Texas, (1891) 83 Tex. 182. The rule established in Dixon County *v.* Field, 111 U. S. 94, and acted upon in Citizens' Bank *v.* Terrell, 78 Tex. 450, was held applicable in such a case. The court said: "If our Constitution were silent upon the subject, then it might reasonably be held that [the following section of the statutes with reference to building court houses, to wit: 'The county shall not issue a larger amount of bonds than a tax of one-fourth of one per cent annually will liquidate in ten years, and said bonds shall only be

the sum authorized under this construction of the constitutional and statutory provisions, the bonds were void; but, having been issued at the same time, each would bear a relative proportion of the loss; and that, as to the excessive issue of these bonds, the purchasers of the bonds could not claim to be innocent purchasers.[1] In an action upon county bonds issued for the construction of bridges, reciting on their face facts as to their issue in conformity to the laws of Colorado upon the subject, one defense was that the bonds were illegal and void, because they increased the indebtedness of the county to an amount in excess of the limit prescribed by the Constitution of the state. The case came before the Supreme Court of the United States upon a certificate which stated that at the time of the issue of the bonds in question the defendant county was in fact indebted beyond the constitutional and statutory limit, and the issue of each bond, therefore, created a debt in excess of that limit; and that the plaintiff bought the bonds upon the faith of the recitals therein, and without making any examination into the facts appearing upon the records of the county. The statute of the state of Colorado required the county commissioners, in submitting the question to a vote of the electors, to enter of record an order specifying the amounts required and the object of the debt; and also made it

sold at their face par or value,'] authorized the Commissioners' Courts to determine the question as to the amount of bonds 'a tax of one-fourth of one per cent annually will liquidate in ten years.' But there being a provision in the Constitution bearing directly upon that subject, we are of the opinion that this section must be construed in connection with it. The limit in the Constitution being an amount upon which a tax of one-half of one per cent would pay annually the interest and two per cent as a sinking fund, and the statutory requirements being such an amount only as one-fourth of one per cent would liquidate in a period of ten years, it was not absolutely necessary that the commissioners should be governed by the same rule in determining the two limits. An amount of indebtedness that would be liquidated within ten years, though based upon a valuation in excess of that shown by the assessment rolls, might still be within the constitutional limit which permits the creation of such a debt as will be ultimately paid by an annual tax of one-half of one per cent upon the taxable values of the county as shown by the official assessment. But we think it more reasonable to presume that the legislature intended that the same rule should govern in determining both limits, and that the Commissioners' Courts should not look beyond the assessment rolls in ascertaining the amount of the indebtedness which the statute authorizes them to create."

[1] Nolan County *v.* The State of Texas, (1891) 83 Tex. 182, following Russell *v.* Cage, 66 Tex. 428; Citizens' Bank *v.* Terrell, 78 Tex. 450.

their duty to publish, and to cause to be entered on their records, open to the inspection of the public at all times, semi-annual statements exhibiting in detail the debts, expenditures and receipts of the county for the preceding six months, and striking the balance so as to show the amount of any deficit and the balance in the treasury. The court held that the holder of these bonds, although a purchaser for value and before the maturity of the bonds, was charged with the duty of examining the record of indebtedness provided for by the statute of Colorado in order to ascertain whether the bonds increased the indebtedness of the county beyond the constitutional limit; and that the recitals did not estop the county to prove by the records of the assessment and the indebtedness that the bonds were issued in violation of the Constitution of the state.[1] The county treasurer of a county

[1] Sutliff *v.* Lake County Comrs., (1893) 147 U. S. 230. Mr. Justice GRAY, speaking for the court, said: "In those cases in which this court has held a municipal corporation to be estopped by recitals in its bonds to assert that they were issued in excess of the limit imposed by the Constitution or statutes of the state, the statutes, as construed by the court, left it to the officers issuing the bonds to determine whether the facts existed which constituted the statutory or constitutional condition precedent, and did not require those facts to be made a matter of public record. Marcy *v.* Oswego, 92 U. S. 637; Humboldt *v.* Long, 92 U. S. 642; Dixon County *v.* Field, 111 U. S. 83; Lake County *v.* Graham, 130 U. S. 674, 682; Chaffee County *v.* Potter, 142 U. S. 355, 363. But if the statute expressly requires those facts to be made a matter of public record, open to the inspection of every one, there can be no implication that it was intended to leave that matter to be determined and concluded, contrary to the facts so recorded, by the officers charged with the duty of issuing the bonds. Accordingly, in Dixon County *v.* Field, 111 U. S. 83, which arose under an article of the Constitution of Nebraska, limiting the power of a county to issue bonds to ten per cent of the assessed valuation of the county, it was adjudged that a county issuing bonds, each reciting that it was one of a series of $87,000 issued under and by virtue of this article of the Constitution and the statutes of Nebraska upon the subject, was not estopped to show by the assessed valuation on the books of public record of the county that the bonds were in excess of the constitutional limit; and Mr. Justice MATTHEWS, delivering the unanimous judgment of the court, fully stated the grounds of the decision, which sufficiently appear by the following extract: 'If the fact necessary to the existence of the authority was by law to be ascertained, not officially by the officers charged with the execution of the power, but by reference to some express and definite record of a public character, then the true meaning of the law would be that the authority to act at all depended upon the actual objective existence of the requisite fact, as shown by the record, and not upon its ascertainment and determination by any one; and the consequence would necessarily follow, that all persons

of the state of New York, under the authority of a resolution of its board of supervisors, and certain statutes then in force, offered for sale and invited bids for bonds of the county aggregating a certain large amount. The bidder in one instance, whose bid was accepted, first gave a check for the sum bid for a certain amount of the bonds, and then stopped payment on the same, and declined to receive them, claiming that the issue of such bonds

claiming under the exercise of such a power might be put to the proof of the fact, made a condition of its lawfulness, notwithstanding any recitals in the instrument.' Dixon County *v.* Field, 111 U. S. 83, 93. In the present case there was no power at all conferred to issue bonds in excess of an amount equal to ten per cent upon the assessed valuation of the taxable property in the county. In determining the limit of power, there were necessarily two factors: The amount of the bonds to be issued, and the amount of the assessed value of the property for purposes of taxation. The amount of the bonds issued was known. It is stated in the recital itself. It was eighty-seven thousand dollars. The holder of each bond was apprised of that fact. The amount of the assessed value of the taxable property in the county is not stated; but, *ex vi termini*, it was ascertainable in one way only, and that was by reference to the assessment itself, a public record equally accessible to all intending purchasers of bonds, as well as to the county officers. This being known, the ratio between the two amounts was fixed by an arithmetical calculation. No recital involving the amount of the assessed taxable valuation of the property to be taxed for the payment of the bonds can take the place of the assessment itself, for it is the amount, as fixed by reference to that record, that is made by the Constitution the standard for measuring the limit of the municipal power. Nothing in the way of inquiry, ascertainment or determination as to that fact is submitted to the county officers. They are bound, it is true, to learn from the assessment what the limit upon their authority is, as a necessary preliminary in the exercise of their functions, and the performance of their duty; but the information is for themselves alone. All the world besides must have it from the same source, and for themselves. The fact, as it is recorded in the assessment itself, is extrinsic and proves itself by inspection, and concludes all determinations that contradict it. Dixon County *v.* Field, 111 U. S. 83, 95." Mr. Justice GRAY then resumed: "That decision and the grounds upon which it rests were approved and affirmed in Lake County *v.* Graham, 130 U. S. 674, and Chaffee County *v.* Potter, 142 U. S. 355, * * * each of which arose under the article of the Constitution of Colorado now in question, but under a different statute, which did not require the amount of the indebtedness of the county to be stated on its record. In Lake County *v.* Graham each bond showed on its face the whole amount of bonds issued, and the recorded valuation of property showed that amount to be in excess of the constitutional limit; and for this reason, as well as because the bonds contained no recital upon that point, the county was held not to be estopped to plead that limit. Lake County *v.* Graham, 130 U. S. 674, 682, 683. In Chaffee County *v.* Potter, on the other hand, the bonds contained an express recital that the total amount

was prohibited by the provision of the State Constitution,[1] which provides that "no county containing a city of over one hundred thousand inhabitants, or any such city, shall be allowed to become indebted for any purpose or in any manner to an amount which, including existing indebtedness, shall exceed ten per centum of the assessed valuation of the real estate of such county or city subject to taxation, as it appeared by the assessment rolls of said county or city on the last assessment for state or county taxes prior to the incurring of such indebtedness; and all indebtedness in excess of such limitation, except such as may now exist, shall be absolutely void, except as herein otherwise provided. No such county or city whose present indebtedness exceeds ten per centum of the assessed valuation of its real estate subject to taxation shall be allowed to become indebted in any further amount until such indebtedness shall be reduced within such limit. This section shall not be construed to prevent the issuing of certificates of indebtedness or revenue bonds issued in anticipation of the collection of taxes for amounts actually contained, or to be contained, in the taxes for the year when such certificates or revenue bonds are issued and payable out of taxes. Nor shall this section be construed to prevent the issue of bonds to provide for the supply of water, but the term of the bonds issued to provide for the supply of water shall not exceed twenty years, and a sinking fund shall be created on the issuing of the said bonds for their redemption, by raising annually a sum which will produce an

of the issue did not exceed the constitutional limit, and did not show on their face the amount of the issue, and the county records showed only the valuation of the property, so that, as observed by Mr. Justice LAMAR, in delivering judgment: 'The purchaser might even know, indeed, it may be admitted that he would be required to know, the assessed valuation of the taxable property of the county, and yet he could not ascertain by reference to one of the bonds and the assessment roll whether the county had exceeded its power, under the Constitution, in the premises.' Chaffee County *v.* Potter, 142 U. S. 355, 363. The case at bar does not fall within Chaffee County *v.* Potter, and cannot be distinguished in principle from Dixon County *v.* Field or from Lake County *v.* Graham. The only difference worthy of note is that in each of these cases the single fact required to be shown by the public record was the valuation of the property of the county. Whereas, here, two facts are to be so shown, the valuation of the property and the amount of the county debt. But, as both these facts are equally required by the statute to be entered on the public records of the county, they are both facts of which all the world is bound to take notice, and as to which, therefore, the county cannot be concluded by any recitals in the bonds."

[1] Const. N. Y. art. 8, § 11.

amount equal to the sum of the principal and interest of said bonds at their maturity." There was a city of more than 100,000 inhabitants in this county. There was a submission of the controversy between the county treasurer and the bidder for these bonds to the Supreme Court of New York in General Term without action. The contention of the bidder was that the constitutional provision should be construed so as to take in the estimate the indebtedness of the city as well as the county in determining the then present indebtedness. The Supreme Court held that under the provision, a city and county in which it was situated might each incur debt to the extent of ten per cent of the assessed value of all the taxable real estate within it; and that the restriction provided by that section was separate and distinct as to each.[1] A case in the federal court for the western district of Iowa involving the validity of certain refunding bonds of a

[1] Adams *v.* East River Savings Institution, (1892) 47 N. Y. St. Repr. 175, holding the bonds valid and authorized and rendering judgment against the bidder. Affirmed in 136 N. Y. 52. The reasoning of the Supreme Court, as to the construction of this provision of the Constitution of New York was approved by the Court of Appeals. CULLEN, J., for the Supreme Court, said: "The first question is, whether the water debt is to be counted in determining whether the ten per cent limit of a city has been reached or exceeded. We think it is. The constitutional provision is that no county or city shall for any purpose go beyond the prescribed percentage. * * * [It is contended] for the defendant that it was the intent of this constitutional provision to restrain the creation of debt either by the city or county which, taken together, would exceed ten per cent of the assessed value of the real estate lying within the county or city; or, in other words, that real estate should not bear the burden of a greater debt both for city and county purposes than ten per cent of its assessed value. * * * 'If the language is unambiguous, the words plain and clear, conveying a distinct idea, there is no occasion to resort to other means of interpretation. Effect must be given to the intent as indicated by the language employed. Especially should this be so in the interpretation of a written Constitution framed deliberately and with care and adopted by the people as the organic law.' Settle *v.* Van Evrea, 49 N. Y. 280. This rule is peculiarly applicable to the case in hand, for the case is singularly barren of external sources from which to draw light. The limit prescribed by the Constitution is wholly arbitrary, and necessarily so. While most citizens would recognize that excessive debts by localities is an evil to be checked, the question of what debt is excessive would produce the widest diversities of opinion; diversities to be composed only by compromise at an arbitrary figure. This is the first provision of the character in any of the Constitutions of this state; so we are equally without tradition or policy in this respect. We must, therefore, decide the case in the very words of the Constitution. The language of the Constitution is dis-

county which had been purchased in good faith, and for a full consideration, by the plaintiff and other purchasers, raised several questions as to refunding bonds. There was abundant evidence to show that the amount received for the bonds was applied by the county through its refunding agent to the payment of bonds then outstanding against the county; also, that the amount of the bonds thus negotiated by its agent exceeded largely the constitutional limitation of five per cent upon the valuation of taxable property of the county, as shown by the last preceding state and county tax lists. The county resisted recovery against it in this action on the ground of the bonds being in excess of the constitutional limitation. The court held that those of the series of bonds which had been issued through the refunding agent of the county, so far as they represented then existing indebtedness of the county at the time they were issued, were valid; those of the series which did not represent such existing indebtedness were held to be invalid.[1]

junctive, 'No county, * * * or any such city, shall be allowed to become indebted to an amount which shall exceed ten per cent of the assessed value of the real estate of such county or city subject to taxation.' The literal and grammatical reading is that the county shall not be allowed to incur debt beyond a certain per cent, and that the city shall not be allowed to incur debt beyond the same per cent. Separate restrictions are imposed on each. This is so clear to my mind as to forbid elaboration."

[1] Ætna Life Insurance Co. *v.* Lyon County, (1890) 44 Fed. Rep. 329, SHIRAS, J., said, generally, as to the bonds: "If this issue of bonds had been negotiated in the purchase of property then acquired. or for the erection of county buildings or other like purposes, so that thereby a new or original indebtedness had been thereby created against the county, there could then be no question that the bonds themselves would be void by reason of the provision of the Constitution of the state of Iowa, limiting the indebtedness of all municipal and political corporations within the state to five per cent upon the taxable property within the limits of the particular corporation; and a recovery thereon could not be had, even in favor of parties who had paid full value therefor in the belief that the bonds were valid. Buchanan *v.* Litchfield, 102 U. S. 278; Dixon County *v.* Field, 111 U. S. 83; s. c., 4 Sup. Ct. Rep. 315; Lake County *v.* Rollins, 130 U. S. 662; s. c., 9 Sup. Ct. Rep. 651; Lake Co. *v.* Graham, 130 U. S. 674; s. c., 9 Sup. Ct. Rep. 654. The bonds in question were not issued for any such purpose, but were issued for the purpose of refunding other outstanding bonds of the county; and the issuance thereof did not in fact increase the indebtedness of the county, but only the form or evidence of the indebtedness. Under these circumstances, it is broadly claimed on behalf of plaintiff that the bonds, being issued to refund or pay other bonds, are not affected by the constitutional limitation. To the extent of holding that, as applied

§ 401. The validity of judgments against a county for which the bonds were issued cannot be questioned in actions on the bonds.— It was argued in behalf of the county in this case upon coupons of the bonds that, upon the issue of unconstitutionality of the issue of the bonds, it was open to the county to question the validity of judgments against the county, or of the bonds issued to fund or pay judgments against the county. The court held that it was not open to the county to make such a defense.[1]

to a series of refunding bonds, the mere fact that the amount thereof might exceed five per cent of the then taxable valuation of the property within the county, as shown by the tax lists, would not necessarily show that the bonds so issued were invalid, I can agree in the views of counsel for plaintiff. If a county owes a valid and enforceable indebtedness, refunding bonds, issued under authority of an act of the legislature for the purpose of taking up such enforceable indebtedness, are not invalid because they may exceed the five per cent limitation. In such case the refunding bonds are valid, because they represent a valid indebtedness. Railroad Co. *v.* County of Osceola, 45 Iowa, 168; Austin *v.* District Tp. of Colony, 51 Iowa, 102. In suits, therefore, upon refunding bonds representing prior indebtedness, it is necessary, in order to sustain the defense of invalidity, to show that the indebtedness merged in and represented by the refunding bonds was itself invalid and non-enforceable either in whole or in part * * *."

[1] Ætna Life Ins. Co. *v.* Lyon County, (1890) 44 Fed. Rep. 329. SHIRAS, J., said: "The constitutional limitation is not self-acting. The protection of its provisions must be invoked at the proper time and in the proper mode. If judgments are obtained against a county, and the same are not reversed, but remain in full force, they are evidence of the highest nature that the county owes the amounts adjudged to be due; and if the county, having the power to fund its outstanding indebtedness, issues bonds in payment of such judgments, the validity of the bonds cannot be successfully attacked, when suit is brought thereon, by showing that, if the defense had been interposed in the original case, the claim might have been defeated, and that the judgment actually rendered might have been prevented. As is said by the Supreme Court in Cromwell *v.* Sac County, 94 U. S. 351: 'Thus, for example, a judgment rendered upon a promissory note is conclusive as to the validity of the instrument, and the amount due upon it, although it be subsequently alleged that perfect defenses actually existed, of which no proof was offered, such as forgery, want of consideration or payment. If such defenses were not presented in the action, and established by competent evidence, the subsequent allegation, if then in existence, is of no legal consequence. The judgment is as conclusive, so far as future proceedings of law are concerned, as though the defenses never existed.' The argument of counsel would have weight if the constitutional provision was to the effect that no judgment could be rendered against a county under any circumstances. In such case, even though a court should enter up a judgment, its unconstitutionality and in

§ 402. The statements of a county's agent in sale of bonds not operative as an estoppel upon the county to defend.—It has been held in a case in the federal court in one of the districts of Iowa that the statements made by the refunding agent of a county in negotiating the sale of certain refunding bonds, which had been issued by a county of that state, did not operate as an estoppel against the county; that it was open to the county to show that the bonds merged into the refunding bonds sold by its agent were in whole or in part invalid and non-enforceable.[1]

validity would be self-apparent, and could always be availed of when its enforcement might be attempted, and this for the reason that upon its face the judgment would show that the court was without jurisdiction. A defense based upon the clause limiting the amount of municipal indebtedness to five per cent upon the amount of taxable property is of a wholly different nature. It requires a proper pleading of the facts, and upon the trial proper evidence must be introduced or else the defense fails. It makes no difference in the validity of the judgment whether the defendant failed to plead the defense based upon the constitutional limitation, or failed to sustain the defense, if pleaded, by sufficient evidence. In either case the rendition of the judgment established the validity of the claim against the county, and the judgment, so long as it remains unreversed, cannot be questioned on the ground that the amount thereof exceeds five per cent of the taxable property of the county."

[1] Ætna Life Insurance Co. *v.* Lyon County, (1890) 44 Fed. Rep. 329. *Arguendo*, it was said by SHIRAS, J.: "When these bonds were offered to the plaintiff it was known to the parties acting for the plaintiff that the series of bonds proposed to be negotiated exceeded in amount five per cent of the taxable property in the county, and, therefore, to authorize the issuance thereof, there must be then in existence a valid indebtedness to the amount of one hundred and twenty thousand dollars, which it was proposed to refund by the issuance of the bonds in question. The validity of the bonds was asserted upon the claim that the bonds to be refunded represented claims that had been reduced to judgment, and, therefore, were enforceable against the county. The purchasers knew, and were bound to know, that unless the assertion was true, the bonds would be invalid, because in excess of the constitutional limitation, and the purchasers were bound to ascertain what the fact in this particular was. The bonds themselves contain no recital on the subject. The certified copy of the proceedings taken by the board of supervisors in regard to the issuance of the bonds, and which copy was submitted to the purchasers, does not contain any statement showing that the bonds proposed to be refunded were based wholly upon prior judgments. The statement relied upon as an estoppel was made by [the refunding agent] first orally and then in the form of an affidavit; but he was not then acting on behalf of the county in ascertaining or certifying to a fact which the law required to be then ascertained and determined as the basis for further action. He was the refunding agent of the county, but he did not have the power to determine any question or matter pertaining to the right to issue the bonds. Dixon Co.

§ 403. **When a county may plead an overissue.**— The United States Circuit Court of Appeals has held in a late case that one who bought municipal bonds at one time in such number as to exceed in amount the limit of the issue authorized by law (being an amount capable of liquidation in a certain time at a given rate of taxation, based on the assessment rolls), was chargeable with notice, and the municipality was not estopped to plead an overissue.[1]

v. Field, 111 U. S. 83; s. c., 4 Sup. Ct. Rep. 315; Daviess Co. *v.* Dickinson, 117 U. S. 657; s. c., 6 Sup. Ct. Rep. 897. The resolution of the board of supervisors appointing [him] declares the object of the appointment to be 'for the purpose of funding and refunding the county indebtedness,' and the resolutions adopted by the board * * * show upon their face that it was the purpose of the board to undertake the bonding of the floating indebtedness, as well as the refunding the then outstanding bonded indebtedness. Upon the question of what the bonds proposed to be refunded were the representative, and whether the same were based upon judgments presumably rendered against the county, the records of the county constituted the primary and best evidence. [The refunding agent] had no charge over or connection with these records, nor was he the one to whom application would naturally be made by one seeking to know the origin and purpose of the outstanding bonded indebtedness of the county. If the effect of an estoppel is given to statements of this character, the protection intended to be secured by the constitutional provision limiting the amount of indebtedness of counties and other municipal corporations would be wholly destroyed. In every instance it could be evaded by the simple device of appointing a refunding agent, and by his statements create an estoppel against the county or city, and thus validate any amount of bonds that might be issued."

[1] Francis *v.* Howard County, (1893) 54 Fed. Rep. 487, affirming Francis *v.* Howard County, (1892) 50 Fed. Rep. 44, in which case MAXEY, D. J., fully discusses the questions involved. *Arguendo,* PARDEE, Circuit Judge, said: "It is contended that the recital in each bond that 'this bond is issued in accordance with the provisions of the act of the legislature of Texas, entitled 'An act to authorize the County Commissioners' Court of the several counties of this state to issue bonds for the erection of a court house, and to levy a tax to pay for the same,' approved February 11, 1881,' is a recital of the performance of a condition precedent, on the part of the County Commissioners' Court, to wit, that the amount of the same was within the limits allowed by the act of 1881, and that a purchaser of the bonds was not bound to inquire, the case being within the principles declared in Marcy *v.* Oswego, 92 U. S. 637; School Dist. *v.* Stone, 106 U. S. 183; s. c., 1 Sup. Ct. Rep. 84, and cases there cited; and particularly in Chaffee County *v.* Potter, 142 U. S. 355; s. c., 12 Sup. Ct. Rep. 216. In the last-mentioned case it was held: 'When there is an express recital upon the face of a municipal bond that the limit of issue prescribed by the State Constitution has not been passed, and the bonds themselves did not show that it had, the holder is not bound to look further.' The answer

§ 404. When the defense that a county was not fully organized when the bonds were issued is not open to the courts.— The United States Supreme Court, in a case involving coupons of bonds issued by a Kansas county for the purpose of building a bridge and court house, held that in that state a county had power to borrow money for such purposes and to issue bonds therefor. Further, it was ruled that when both the executive and legislative departments of the state had given notice to the world that a county within the terrritorial limits of that state had been duly organized and existed, with full power of contracting, it was not open to the courts to dispute those facts in an action brought against it by a holder of its bonds, who bought them in good faith in open market. The debts of a county, contracted during a valid organization, remain the obligations of the county, although for a time the organization may be abandoned, and there be no officers to be reached by the process of the court. Further, a recital in a bond of a municipal corporation in Kansas that it was issued in accordance with authority conferred by the act of March 2, 1872 (Kansas Laws, 1872, 110, chap. 68), and in accordance with a vote of the majority of the qualified voters, was held sufficient to validate the bonds in the hands of a *bona fide* holder; and the certificate of the auditor of the state thereon that the bond was regularly issued; that the signatures were genuine, and that the bond had been duly registered, was conclusive upon the municipality. Also, a recital on a bond issued by a county in Kansas for the purpose of building a bridge, need not necessarily refer to the particular bridge for the construction of which it was

to this contention of the plaintiff in error is that the recital in the bonds sued on is not a recital of facts so much as of a conclusion of law; that the bonds contain no express recital of the existence of any fact, and that a fair construction of the act of 1881 leaves the ascertainment of no fact to be found by the County Commissioners' Court as a condition precedent to the issue of bonds themselves, but practically leaves the County Commissioners' Court and all purchasers and holders of bonds to act at their peril. All of the decisions of the Supreme Court of the United States, from Dixon Co. *v.* Field, 111 U. S. 83; s. c., 4 Sup. Ct. Rep. 315, to Sutliff *v.* Board, 147 U. S. 230; s. c., 13 Sup. Ct. Rep. 318, agree that the purchasers of bonds issued by municipalities under authority of laws which limit the amount of bonds to be issued to a certain percentage of the assessment rolls, or to a given rate of taxation based on such rolls, are charged with notice of the assessment rolls, and of the amount of bonds which can be validly issued, based on such assessment rolls."

issued.[1] In a late case before the United States Circuit Court of Appeals it appeared that after the organization of a new county in Michigan, under an act of the legislature of 1871, its board of supervisors determined that it required a certain amount of money to erect a court house and jail, and, after a vote of the citizens in favor of it, raised the amount by issuing county bonds and selling them to *bona fide* purchasers for value. These bonds were afterwards paid in part and reduced to judgment in part by the holders. The money raised by the sale of these bonds had been used for the purposes of erecting the county court house and the jail, and the latter used for the purposes of the county. In 1875 another act was passed organizing the county. In 1885 an act was passed which authorized the refunding of outstanding bonds of the county, and the bonds originally issued and judgments upon such as had been sued were surrendered by the holder and these refunding bonds given in exchange. Upon the latter bonds this action was brought, and the Circuit Court, presumably upon its idea of the effect of a decision of the state Supreme Court in a certain case, upon the defense that the county was not organized as the Constitution of the state required, directed a judgment in favor of the county. The United States Court of Appeals reversed the Circuit Court, and held the bonds for which these refunding bonds were exchanged to have been valid obligations of the county.[2]

[1] Comanche County *v.* Lewis, (1890) 133 U. S. 198, affirming Lewis *v.* Comanche County, 35 Fed. Rep. 343. As supporting the third point, see State ex rel. *v.* Yoxall, 40 Kans. 323; Broughton *v.* Pensacola, 93 U. S. 266; Mount Pleasant *v.* Beckwith, 100 U. S. 514. As to the effect of the recitals, see School District *v.* Stone, 106 U. S. 183; Lewis *v.* Commissioners, 105 U. S. 739. As to the power of Kansas counties to borrow money and issue bonds, see Leavenworth County *v.* Miller, 7 Kans. 479; Doty *v.* Ellsbree, 11 Kans. 209.

[2] Ashley *v.* Board of Supervisors of Presque Isle County, (1893) 60 Fed. Rep. 55. It was said by the court; "We do not consider the act of 1875 as in any sense a repudiation of the original organization. Doubts had arisen in regard to its legality. The public interests required that those doubts should be put at rest, and the legislature proceeded to clothe the county with an unquestionable title. Having regard to what transpired, it would seem that the statute should be regarded as effecting a reorganization and giving express sanction for the continuance of a body whose origin was clouded with doubts of its lawfulness. However that might be, the statute could not, upon any construction, operate to divest rights which had been acquired while the county was exercising the powers it had assumed."

§ 405. **Counties suable in federal courts.**— It was claimed in an action upon the bond of a county in Nevada that because a county was an integral part of the state it could not, under the eleventh amendment of the Federal Constitution, be sued in the United States Circuit Court; also, that inasmuch as the act under which the bonds were issued provided for litigation concerning the court, and named the court of the state in which such litigation could be had, that such jurisdiction was exclusive, and prevented suit in the Circuit Court. The United States Supreme Court held adversely to both of these contentions.[1]

§ 406. **Plea of Statute of Limitations on county bonds.**— In this action upon bonds of a county in Nevada the county

[1] Lincoln County *v.* Luning, (1890) 133 U. S. 529. Mr. Justice BREWER, speaking for the court, said: "With regard to the first objection, it may be observed that the records of this court for the last thirty years are full of suits against counties, and it would seem as though by general consent the jurisdiction of the federal courts in such suits had become established. But irrespective of this general acquiescence, the jurisdiction of the Circuit Courts is beyond question. The eleventh amendment limits the jurisdiction only as to suits against a state. It was said by Chief Justice MARSHALL, in Osborn *v.* Bank of the United States, 9 Wheat. 738, 857, that the 'eleventh amendment, while restraining the jurisdiction granted by the Constitution over suits against states, is of necessity limited to those suits in which the state is a party on the record. While that statement was held by this court in the case of In re Ayers, 123 U. S. 443, to be too narrow, yet by that decision the jurisdiction was limited only in respect to those cases in which the state is a real, if not a nominal defendant; and while the county is territorially a part of the state, yet politically it is also a corporation created by and with such powers as are given to it by the state. In this respect it is a part of the state only in that remote sense in which any city, town, or other municipal corporation may be said to be a part of the state. Metropolitan Railroad Co. *v.* District of Columbia, 132 U. S. 1. * * * With regard to the other objection, the case of Cowles *v.* Mercer County, 7 Wall. 118, 122, is decisive. In that case the court, by the chief justice, expressed its opinion on the very question in these words: 'But it was argued that counties in Illinois, by the law of their organization, were exempted from suit elsewhere than in the Circuit Courts of the county. And this seems to be the construction given to the statutes concerning counties by the Supreme Court of Illinois. But that court has never decided that a county in Illinois is exempted from liability to suit in national courts. It is unnecessary, therefore, to consider what would be the effect of such a decision. It is enough for this case that we find the board of supervisors to be a corporation authorized to contract for the county. The power to contract with citizens of other states implies liability to suits by citizens of other states, and no statute limitation of suability can defeat a jurisdiction given by the Constitution.'"

attempted to avail itself of the Statute of Limitations. The United States Supreme Court held that when, after default by a municipal corporation in the payment of interest upon its bonds, the legislature provides for the creation of a special fund by the debtor out of which the creditor is to be paid, the debtor cannot set up the Statute of Limitations to an action on the bonds and coupons without showing that the fund had been provided.[1]

§ 407. **When statute as to presentation of claims is not applicable to judgments upon bonds and coupons.**—The statute of Nevada requiring presentation of claims and accounts against counties to the county commissioners and county auditor

[1] Lincoln County *v.* Luning, (1890) 133 U. S. 529. The bonds in this case had been issued in 1873. In 1877 the county was delinquent in its interest, and there was an amendatory act passed providing for the registration of overdue coupons and imposing upon the treasurer the duty of thereafter paying the company as money came into his possession applicable thereto. It was said by the court: "The coupons, which by the General Limitation Law would have been barred, were presented as they fell due to the treasurer for payment and payment demanded and refused because the interest fund was exhausted. Thereupon the treasurer registered them as presented in accordance with the act of 1877, and from the time of their registration to the commencement of this suit there was no money in the treasury applicable to their payment. This act, providing for registration and for payment in a particular order, was a new provision for the payment of these bonds, which was accepted by the creditor and created a new right upon which he might rely. It provided, as it were, a special trust fund to which the coupon holder might, in the order of registration, look for payment and for payment through which he might safely wait. It amounted to a promise on the part of the county to pay such coupons as were registered in the order of their registration as fast as money came into the interest fund; and such promise was by the creditor accepted. * * * The cases of Underhill *v.* Sonora, 17 Cal. 173, and Freehill *v.* Chamberlain, 65 Cal. 603, are in point. In the former case the court observes that 'the legislative acts then recognized the debt and made provision for its payment. This is enough to withdraw the case from the operation of the statute; it is equivalent to a trust deed by the state setting apart property out of which the money due was to be paid at a given time, if not sooner paid upon a claim acknowledged to be an outstanding debt; and we cannot conceive of any principle of law or justice which would hold the claim to be barred by the statute simply because the creditor waited after this for his money.' In the other case it was held that 'where a statute provides for the issuing of bonds of a city with interest coupons payable as fast as money should come into the treasury from special sources designated by the act, the Statute of Limitations does not commence to run against the coupons until the money is received in the treasury in accordance with the terms of the act.'"

for allowance and approval has been held by the federal court for that district to apply only to unliquidated claims and accounts, not to bonds and coupons, nor to a judgment upon bonds and coupons. Neither is such presentation necessary before an action on such a judgment. It was further held that where the statute authorizing bonds to be issued provides for their payment by levying a special tax and creating a special fund, an allowance by a county board and audit of a claim on a judgment on such bonds as payable out of the general fund, would not be an allowance in the manner and form to which the holder would be entitled; nor would he be precluded from maintaining an action on the judgment because of another remedy prescribed by statute to enforce payment of claims allowed and audited.[1]

§ 408. **The proper proceeding of courts where some of the bonds of a series are valid and others invalid.**—A corporation holding certain of a series of refunding bonds issued by a county in Iowa, having brought its action at law in the federal court of one of the districts of that state, and the court holding some of the bonds of the series valid and some invalid, the court was compelled to order judgment in favor of the county because it was not possible in the action to settle the equities of the different holders of these bonds. The judgment was, however,

[1] Vincent *v.* Lincoln Co., (1894) 62 Fed. Rep. 705. The court said: "The judgment originally obtained in this case and upon which this action is brought is conclusive that the bonds and coupons upon which the judgment was rendered were binding obligations, which entitled plaintiff to payment of the same out of the fund created by law for that purpose or out of any fund that could be lawfully created for the payment of the same. And it is not within the power of the board to limit this right so as to deprive plaintiff of the remedy to which he is entitled under the law. Ralls Co. Court *v.* U. S., 105 U. S. 733, and note; Lincoln Co. Court *v.* U. S., 105 U. S. 739, note." That the complaint on coupons and bonds of a county is not defective for not showing that they had been presented to the county commissioners and county auditor for allowance and approval as provided in statutes of the state, see County of Greene *v.* Daniel, 102 U. S. 187, 194, in which the court observed, speaking of bond and coupons, that "the claim was, to all intents and purposes, audited by the court when the bonds were issued. The validity and the amount of the liability were then definitely fixed and warrants on the treasury given, payable at a future day." As to the constitutionality of the statute of Nevada authorizing the issue of certain county bonds, see Odd Fellows' Bank *v.* Quillen, 11 Nev. 109, following Youngs *v.* Hall, 9 Nev. 212; approved and followed in Lincoln County *v.* Luning, (1890) 133 U. S. 529, 532.

without prejudice to the plaintiff, leaving it in its power to bring an action of equity to settle the equities of the holders, which the court recognized. As to the inability of the court at law, SHIRAS, J., said: "It is argued that the bonds would be valid until the amount needed to refund the enforceable debt had been reached, and that it will be presumed that the bonds were sold in the order of their number. Such a presumption cannot be indulged in under the facts of this case. To settle the equities and rights of the bondholders against the county and their rights as between themselves would seem to require the institution of a suit in equity. In this action at law between one owner of part of the bonds and the county, it is beyond the power of the court to hear and determine the question of the order in which the series of bonds were sold or the application of the proceeds realized from the sales thereof, and whether the facts are such that a certain number of the bonds can be held valid at law, or whether it should not be held that each owner of a bond is equitably entitled to demand his share of the total sum which may be adjudged to be collectible from the county." He suggested the following as a proceeding proper in such a case: "It seems to me that the only means of solving the difficulties of the situation is for the plaintiff and the other non-resident bondholders to unite in a proper proceeding in equity against the county and such other bondholders as may refuse to act as complainants, and in such suit it can finally be determined for what amount the county can be held liable and the rights of the respective bondholders in and to this sum can be decreed." [1]

[1] Ætna Life Insurance Co. *v.* Lyon County, (1890) 44 Fed. Rep. 329, 345.

CHAPTER XIX.

CITY BONDS.

§ 409. City bonds generally.
410. Extension of a bonded debt of a city.
411. Bonds for funding indebtedness.
412. Effect of a statutory limitation on bonds.
413. Bonds in compromise of outstanding indebtedness.
414. The effect of a statute legalizing an issue of bonds.
415. Bonds for public improvements—limitations on power to issue.
§ 416. Effect of an order by resolution of council of a city for an election to authorize the issue of bonds.
417. Bonds valid when issued as a part of the general indebtedness of a city.
418. Validity of bonds as affected by a restriction in the charter of a city.

§ 409. **City bonds generally.**—The weight of authority upon the power of a municipal corporation to execute bonds, to be placed on the market for the purpose of raising money to be expended by the agents of the corporation, or for the purpose of funding outstanding indebtedness, seems to be generally against the exercise of the power except in cases where the power is derived from legislative authority, expressed or implied. The reason for the ruling is well known to be in the fact that municipal corporations are established to enable the people residing in towns and cities to have the benefits of local government. Unlike trading or business corporations, their powers, unless otherwise directed by express or implied grant, should be, and are, in law as well as in public policy, limited to such as are governmental or administrative in their nature and scope, to such as are necessary to conserve the purposes of their organism.[1] Where a city had power to borrow money to assist in construction of certain improvements, and did so borrow, but a portion of the sum was misappropriated, the Indiana Supreme Court held that the city had power to borrow an additional amount by issuance of bonds to pay the residue of the debts unpaid.[2] Municipal bonds, in the absence of statutory authority, can only be payable at the municipal treasury.[3] The Indiana statute conferring on cities the

[1] Holmes *v.* City of Shreveport, (1887) 31 Fed. Rep. 113.

[2] Daily *v.* City of Columbus, 49 Ind. 169.

[3] Sherlock *v.* Village of Winnetka, 68 Ill. 530.

general power, without restriction, to purchase real estate for the purpose of constructing buildings thereon, has been held to give by implication the exclusive right to determine the expediency of the purpose, the power to purchase on credit and to issue necessary bonds for the purchase money.[1] A city will not be prevented from issuing new bonds with coupons for future interest, for the purpose of funding debts, with accrued interest, existing prior to the adoption of a constitutional provision prohibiting municipal corporations from becoming indebted to an amount in the aggregate exceeding two per centum on the value of their taxable property by such provision.[2] A citizen and taxpayer of a city may by injunction prevent the issue of negotiable bonds which *bona fide* holders might enforce, and, where they have been issued, but remain in the hands of one who received them with notice, may maintain a suit to restrain their transfer, and for their surrender and cancellation.[3] A city authorized to issue a bond for its indebtedness, the Supreme Court of Illinois held was authorized to issue another bond upon terms as to interest within the limitations of its charter in that respect, upon the coming due of the first bond issued, for the time extended, and take up the old one therewith.[4] The onus of showing that bonds issued by a municipal corporation are illegal is on the one who seeks to impeach them.[5] A *bona fide* holder of bonds of a municipal corporation, where the corporation has power under any circumstances to issue negotiable securities, has a right to presume that they were issued under circumstances giving the requisite authority, and such bonds are no more liable to be impeached in the hands of such a holder than any other commercial paper.[6] An innocent holder, acquiring municipal bonds, without collusion, for a valuable consideration, will not be prejudiced by irregularities in their issue where he had no knowledge of such irregularities.[7] The defense that one is the *bona fide* holder may be set up when bonds are made negotiable, or when coupons are detached from

[1] City of Richmond *v.* McGirr, 78 Ind. 192.

[2] Powell *v.* City of Madison, 107 Ind. 106.

[3] City of Madison *v.* Smith, 83 Ind. 502. As to the power of Kansas cities to issue bonds in payment of the building of sidewalks, see Wyandotte *v.* Zeitz, 21 Kans. 649.

[4] City of Quincy *v.* Warfield, (1861) 25 Ill. 320.

[5] Ibid.

[6] Gelpcke *v.* Dubuque, 1 Wall. 175.

[7] State *v.* City Council, 74 Ala. 226; Burr *v.* City of Carbondale, 76 Ill. 455; Town of Douglas *v.* Niantic Savings Bank, 97 Ill. 228.

the bonds, the coupons being negotiable.[1] An act authorizing the issue of bonds of a city in Alabama for the construction of a canal, etc., declared that "No bond shall be issued but upon an entire concurrence of the board of mayor and aldermen, upon a full attendance of all the members of the board, and when there is no vacancy, which shall be made manifest only by an entry of the order for issuing being made on the minutes of the board, and signed by each member thereof; nor shall any contract amounting to one hundred dollars, made under any of the provisions of this act, be valid, which is not made under all the restrictions in this section recited." This restriction was held to continue under an act subsequently passed extending the amount and authorizing the money to be appropriated under the supervision of the mayor and aldermen "for any purpose of internal improvement for the benefit of the citizens of [the city]." And a purchaser of a bond issued under this last act, and reciting on its face that it was so issued, was held chargeable with notice of the restrictions and conditions and not entitled to claim protection as an innocent holder, although the bond also recited that it was issued in conformity with the statute.[2] A clause in the charter of an Illinois city empowering the city council to borrow money not exceeding $100,000, and issue bonds therefor, has been held to apply to the incurring of liabilities by borrowing money and not to those incurred as a part of the current expenses of the city.[3] A third person liable to pay to a municipal corporation the indebtedness, for instance, a judgment for which the corporation has issued bonds in payment of in favor of the judgment creditor, cannot set up the fact that the bonds were invalid by reason of being in excess of the constitutional limit of indebtedness.[4] The existing legal power or authority to issue municipal bonds being defectively or irregularly executed, makes the bonds only voidable.[5] Municipal bonds

[1] Atchison *v.* Butcher, 3 Kans. 121.

[2] Mayor *v.* Wetumpka Wharf Co., 63 Ala. 611. An illustration of when the holder of coupons of bonds void as *ultra vires* the corporation to issue, cannot maintain a suit against a city treasurer for taxes levied for the payment of these coupons under an ordinance of the council of the city and coming into the hands of the treasurer. McConnell *v.* Hamm, 16 Kans. 228.

[3] Barrett *v.* City of East St. Louis, 89 Ill. 175, holding a bond issued in payment of a current liability valid, although the bonded indebtedness of the city exceeded the limitation stated in the text.

[4] Sioux City *v.* Weare, 59 Iowa, 95.

[5] Ryan *v.* Lynch, 68 Ill. 160.

merely voidable may be enforced in the hands of an innocent purchaser for value, but if they are absolutely void, they cannot be enforced, either by the original holder or a purchaser for value.[1] Even in the hands of an innocent holder, bonds of a municipal corporation issued without authority, are void.[2]

§ 410. **Extension of a bonded debt of a city.**— The question raised in a New York case was over an apparent collision between the terms of the charter of a city and the Refunding Act of 1878. The charter had in it these words of restraint upon the city: "The common council shall not have power to borrow, and is hereby expressly prohibited from borrowing, any money on account of the city, except as herein provided. The said council shall not create any pecuniary obligations whatever on the part of the city which shall not be payable in the current year, and which cannot be discharged from the income of the same year." Nevertheless a bonded debt was lawfully created to supply the city with water; not by an amendment of the charter, but by express legislative permission outside of it, granting authority to borrow money for such purpose, and that permission was given without notice of or reference to the section of the charter prohibiting a loan. FINCH, J., for the Court of Appeals, said of it: "It operated as a specific exception to an established general rule, and, so construed, the two acts could be read together without collision or contradiction." The Refunding Act, passed afterwards, authorized in two forms the extension of a bonded debt for a period not exceeding thirty years, but at a lower rate of interest. This act applied to every village, city or county owing such debt and desiring to extend it through an added period of credit. It applied to all of them without refer-

[1] Barnes *v.* Town of Lacon, 84 Ill. 461.

[2] Williamson *v.* Keokuk, 44 Iowa, 88. That bonds of municipal corporations issued without legal authority, are void even in the hands of innocent purchasers without actual notice of the want of power in the corporation to issue them, see Bissell *v.* City of Kankakee, 64 Ill. 249; Livingston County *v.* Weider, 64 Ill. 427; Town of Big Grove *v.* Wells, 65 Ill. 263; Ryan *v.* Lynch, 68 Ill. 160. As to the power of a city in Michigan to issue bonds without a vote of the electors, see Common Council of City of Muskegon *v.* Gow, (1892) 94 Mich. 453; s. c., 54 N. W. Rep. 170. As to authority to issue, see Tillotson *v.* City of Saginaw, (1892) 94 Mich. 240; s. c., 54 N. W. Rep. 162. As to city revenue bonds, see People *v.* Myers, (1893) 138 N. Y. 590.

ence to their charters or the acts under which the indebtedness was created, and was an enabling act of which any city might avail itself. The two forms of extension authorized were, *first*, an exchange of old for new bonds, securing the new credit at the lower rate of interest, and, *second*, to meet the emergency of a refusal by holders to make the exchange bond for bond, the issue and sale of new bonds, applying the proceeds to the cancellation of the old ones. The city involved in this case chose the second form of extension, and the purchaser refused to take the new bonds, upon the ground that it was a borrowing of money prohibited by the charter, and the issue of the bonds by the city was unauthorized. The Court of Appeals affirmed the decree of the court below that the purchaser should specifically perform his part of the contract to purchase these bonds, holding the bonds valid and authorized.[1]

[1] City of Poughkeepsie *v.* Quintard, (1892) 136 N. Y. 275. FINCH, J., speaking for the court, said: "It must be conceded that the transaction in form may be a borrowing of money, but in substance it is the very different case of refunding an existing debt. There is a new creditor and a new rate of interest, but the same old debt. The municipal liability is not increased, but merely suffered to remain, and not a dollar of new or added debt results. The transaction is no different from what it would have been if there had been an exchange of bonds. There it is conceded there would have been no borrowing of money, and merely an extension of credit. But the actual result and the contemplated purpose are exactly the same under the second form of refunding as under the first, and I do not think the permission of the Enabling Act comes into collision with the prohibition of the charter. That prohibition had an obvious purpose and meaning. It was to restrain the creation of a debt, not the extension of one already existing; to prevent a new liability, not to postpone payment of an old one; to shield the taxpayers from the waste and danger of extravagant and needless appropriations, and not to obstruct the convenient and beneficial extension of a proper debt lawfully incurred. Full force and effect can be given to each statute by reading them together, and construing them as if they were contained in one and the same act of legislation. It is our duty to harmonize them if possible, and I can see no more reason for deeming them inconsistent and repugnant than the provision of the charter and the original act authorizing the water debt. It is true that the Refunding Act is a general act, applying to all the municipalities, and that circumstance is urged to show that it worked no repeal of the debt provision of the charter, but no repeal was necessary or intended. Here was in the Refunding Act a specific permission to do one particular thing granted to all cities and so given to [the one here], and that particular intention to allow the refunding of its maturing debt is met by the general intention manifested in the charter, not to permit any debt to be contracted at all, and in such a case, if there be inconsistency, the particular intention takes effect as an exception. Hoey *v.*

§ 411. **Bonds for funding indebtedness.**— A city of Missouri had authority in law to borrow money within a certain limitation as to interest, and to provide for the payment of its debts. An ordinance was passed by the council creating the office of "city fund commissioner," and it was made his duty to sell the bonds of the city for the purpose of funding or paying the indebtedness of the city, and apply the proceeds to the purchase of outstanding warrants and bonds past due, or not having more than three years to run. By this ordinance he was limited in his sales to a price not less than ninety-five cents on the dollar of the par value of five-year bonds, and ninety cents for those running ten years. Upon his report of the amount of the city's indebtedness at a certain date, and how much of it was about to mature, an ordinance was passed authorizing him "to negotiate the bonds of the city for the purpose of raising money to liquidate the city debt, for a period not exceeding fifteen years, and at a rate of discount not exceeding fifteen per cent." On the 28th of March, 1872, the general assembly of Missouri passed an act providing for the registration of bonds issued by counties, cities and incorporated towns. The city, after the passage of this act, issued bonds for the purpose of raising money to pay its interest-bearing debts and the expenses of its government, containing recitals that they were issued under the authority of the charter and the ordinance above referred to. These bonds were executed after the act of March 28, 1872, went into effect, but were antedated for the purpose of evading the provisions of that statute. Without being registered these bonds were placed by the city fund commissioner in the hands of a stock and bondbroker of character for sale. This broker

Gilroy, 129 N. Y. 132. But I do not think that the refunding provision is within the spirit or intent of the charter prohibition. The object and purpose of the latter was to prevent something entirely different in substance and effect from that which the Refunding Act permitted, and the two statutes may be read together, and each perform its proper office and accomplish its appropriate duty without necessary collision or inconsistency. Nor do we encounter difficulty in the provisions of the charter, which point out the mode of payment, and provide for the payment itself of a matured debt. They operate only when ultimate payment is required, and have no application when, by the extension of the debt, its payment is postponed in fact. What may seem payment in form is not so in truth, but a mode of substituting extended bonds for those matured, taking the form of payment solely to compel the substitution intended. I think substance would be sacrificed to form, the intention of one statute be defeated, and of the other perverted, if we should construe them as hostile and inconsistent."

sold certain of the bonds to persons who paid to the broker ninety per cent of their face value, the price in money, the purchasers being ignorant of the fact that the bonds were actually executed after the registration law went into effect, or that the recitals were not in all respects true. They bought and paid for them in good faith, believing them to be what on their face the bonds purported to be and obligatory on the city. The broker, by his agreement with the fund commissioner, retained from the money realized on the sales five per cent on the par value of the bonds sold for his services, and paid the residue to the fund commissioner, who, with the sanction of the city council, used part in the payment and redemption of matured bonds, coupons and warrants of the city, and handed over the rest to the city treasurer. The fund commissioner charged himself with eighty-five per cent of the par value of these bonds, as the sum realized by him, and it was used for city purposes. The city met the interest for a while and then repudiated the bonds. The United States Supreme Court held that the holder of the bonds could recover the money which had been paid for them; that the right of action, though the bonds were invalid, could be sustained as an action for money paid by mistake, or upon a consideration which happens to fail, or for money got through imposition.[1] A late case in the United States Circuit Court for the district of Indiana shows the following facts: The city advertised for bids for a whole or a part of a certain amount of its "refunding bonds of 1893." A firm which was the successful bidder for the whole amount deposited a sum of money in a bank and took a certificate of deposit, payable to the city officials. The money was to be returned on the completion of the purchase, and to be forfeited in case the bidders failed to complete it. The firm, discovering that a portion of the bonds were invalid, brought their action against the city and the bank to obtain a return of the

[1] Louisiana *v.* Wood, (1880) 102 U. S. 294. The court said: "The money was paid for bonds apparently well executed, when in fact they were not, because of the false date they bore. This was clearly money paid by mistake. The consideration on which the payment was made has failed, because the bonds were not in fact valid obligations of the city. And the money was got through imposition, because the city, with intent to deceive, pretended that the false date the bonds bore was the true one. While, therefore, the bonds cannot be enforced because defectively executed, the money paid for them may be recovered back."

certificate of deposit and a decree entitling them to the money. A section of the charter was in these words: "The common council shall have power to authorize the issue and sale of refunding bonds in order to raise money to take up any outstanding bonds of said city, or to exchange with the holders of such outstanding bonds. The same shall be governed by the provisions of the second preceding section, so far as the same are applicable." "In view of the language of section 33," said the court, "there is no room for doubt in regard to the securities embraced in the words 'refunding bonds.' The language of the statute contains its own interpretation. Refunding bonds are of two sorts: *First*, those which are issued and sold to raise money to take up outstanding bonds of the city, or, *second*, those which are issued by the city to the holders of its outstanding bonds in exchange therefor. By the express terms of the statute refunding bonds cannot lawfully be issued for any other purpose. Six hundred of the bonds * * * awarded to the complainants were to be issued and sold to raise money to pay off and take up a like amount of the outstanding bonds of the city. To this extent and for this purpose the city had the undoubted authority to issue and sell its bonds."[1] It was held, however, that the bonds to the amount of $21,000 included in the issue over and above the $600,000 which were issued for the purpose of replacing in the general treasury of the city, which had been long before paid out in extinguishment of a series of bonds issued for the purchase of a farm, were not refunding bonds, and, therefore, not within the terms of the complainants' bid nor the city's award; that these bonds, as refunding bonds, were *ultra vires* and void, and a decree was ordered in favor of the complainants on the ground that they were entitled to stand upon the terms of their bid and entitled to a series of bonds issued solely as refunding bonds.[2]

§ 412. **Effect of a statutory limitation on bonds.**— A city of New York of more than 100,000 inhabitants was authorized by the legislature to issue bonds not to exceed a certain amount at a rate of interest not greater than four per cent and payable in not more than fifty years, in order with the proceeds to improve and extend its water supply. The city issued a part of the authorized bonds and put them on the market at public sale to the highest bidder.

[1] Coffin *v.* City of Indianapolis, (1894) 59 Fed. Rep. 221.

[2] Ibid.

One purchaser refused to accept and pay for the bonds he had bid for, upon the ground that the city could not, under the constitutional restrictions, issue the bonds redeemable in fifty years, which was the term of credit stipulated, but was confined to an issue running but twenty years and accompanied by a sinking fund sufficient to extinguish the debt at its maturity. In an action by the city against the purchaser, the New York Court of Appeals affirmed the judgment in favor of the city, sustaining the validity of the bonds as issued.[1]

[1] City of Rochester *v.* Quintard, (1892) 136 N. Y. 221, affirming 65 Hun, 460; See, also, Sweet *v.* City of Syracuse, 129 N. Y. 316. Cases holding the bonds of the city valid commercial securities: Holmes *v.* City of Shreveport, 31 Fed. Rep. 113; Dorian *v.* City of Shreveport, 28 Fed. Rep. 287; Oubre *v.* Donaldsonville, 33 La. Ann. 386; Reynolds *v.* Shreveport, 13 La. Ann. 426; City of Austin *v.* Nalle, (1893) 85 Tex. 520; s. c., 22 S. W. Rep. 668; De Mattos *v.* City of New Whatcom, (1892) 4 Wash. St. 127. In Portsmouth Savings Bank *v.* Village of Ashley, (1892) 91 Mich. 670, steps had been taken under the statute authorizing the issue of water works bonds for such an issue; after the vote of the citizens upon the question a series of bonds were signed by the president and clerk of the village, and placed in the hands of the president of a railroad company, as appeared in the action, for sale by him, the proceeds to be used for the benefit of the railroad company in consideration of an agreement to complete the road to the village. The bonds not being of a good appearance, another set of bonds were issued in their stead, the interest being made payable at a bank, so as to render them more salable. They were then sold to a bank which brought this action upon coupons of the bonds, claiming to be a *bona fide* purchaser. The Supreme Court of the state held that the statute of Michigan, with reference to the issue of water works bonds, vested the power in the village council, and until that body had met in a legal meeting and voted to issue the bonds, or authorized their issuance, one of the essential requirements of the statute had not been complied with; and that a resolution of the village council, authorizing the president and clerk to sign water works bonds, conferred no authority upon those officers to issue and dispose of the bonds, and if issued and disposed of without such authority, they were not binding on the village. See, on the subject of the right of holders of bonds in such cases, Brown *v.* Bon Homme County, (S. D.) 46 N. W. Rep. 173; Coler *v.* Cleburne, 131 U. S. 162; Bank *v.* Bergen County, 115 U. S. 384; Ledwich *v.* McKim, 53 N. Y. 315; McGarrahan *v.* Mining Co., 96 U. S. 316. As to the rights of a holder of bonds to stand in the place of the party to whom they were issued and recover, though the security may be invalid upon a count for money had and received or for money paid by mistake, see People *v.* Supervisors, 11 Cal. 170; Sturtevant *v.* Liberty, 46 Me. 457; Smith *v.* Cheshire, 13 Gray, 318; Brewster *v.* Hyde, 7 N. H. 208; Moore *v.* Sinks, 2 Ind. 257; Inhabitants, etc., *v.* Weir, 9 Ind. 224; Willim *v.* Bernheimer, 5 Minn. 290; Simms *v.* Hervey, 19 Iowa, 288; Wood *v.* Louisiana, 3 Dill. 122; Gause *v.* Clarksville, 5 Dill. 180; Paul *v.* City of Kenosha, 22 Wis.

§ 413. **Bonds in compromise of outstanding indebtedness.** — Upon the bonds issued by a Kansas city of the second class there were recitals to this effect: "That they were executed and issued by the city to compromise and refund its matured and maturing indebtedness heretofore legally created by said city and in accordance with the above-named act of 1879 [the act which authorized a refunding of the city's indebtedness]." "And it is hereby certified that the total amount of this issue of bonds does not exceed the actual amount of the outstanding indebtedness of said city, and that all the requirements of the provisions of the foregoing act have been strictly complied with in issuing this bond." They were signed by the mayor, and attested by the city clerk under the seal of the city. The federal court for the district of Kansas, in an action upon the bonds, held that under the provisions of the Kansas statute, that the powers granted to such cities "shall be exercised by the mayor and council of such cities," and which directs that funding bonds shall be duly issued only after an ordinance therefor shall be duly passed, these bonds which had been issued without any ordinance or resolution of the mayor and council, were void. Neither was the city estopped by the recital in the bonds to the effect that all the requirements of the statutes had been strictly complied with from denying their validity.[1]

266; Wilkinson *v.* Babbitt, 4 Dill. 208; Oneida Bank *v.* Ontario Bank, 21 N. Y. 490.

[1] Swan *v.* City of Arkansas City, (1894) 61 Fed. Rep. 478. In the opinion, the holders were considered innocent holders of the bonds, with all the rights of such, under the authority of Porter *v.* Steel Co., 122 U. S. 267; s. c., 7 Sup. Ct. Rep. 1206; Scotland Co. *v.* Hill, 132 U. S. 107; s. c., 10 Sup. Ct. Rep. 26, and it was said: "Plaintiffs are, therefore, entitled to all the protection which the law gives to holders of this class of securities, who purchased them without notice and for value. Since the decision of the Supreme Court in the Knox Co. Case, 21 How. 539, it is the settled doctrine of the United States courts that, in an action on municipal bonds by an innocent holder, the municipality will be estopped to deny the truth of all recitals contained in the bonds which the officers issuing them were, by law, to determine before issuing the bonds. But this does not affect the power of the corporation or its officers to issue the bonds. No recitals can estop the municipality from pleading a want of power to issue the bonds, for the reason that municipalities and the officers thereof are but agents with limited powers, and their authority to act must be found in the public acts, and will not be presumed to exist. * * *" The plaintiffs urged that the recitals, "that all the requirements of the provisions of the act have been strictly complied with in issuing them," makes it unnecessary for a purchaser to examine the public records of the city

§ 414. The effect of a statute legalizing an issue of bonds.— The bonds of a city of Nebraska issued to raise money to erect a high school building, being in excess of the amount which the city, by the then existing legislation, was authorized to issue, were legalized by an act of the legislature subsequently passed. In an action by a holder, upon coupons detached from the bonds due and unpaid, it was contended that the act legalizing the bonds, by legalizing bonds void because the city had no power to issue them, was, in law, equivalent to an act conferring upon the city power to issue bonds, which was conferring corporate power, and being a special act was, therefore, unconstitutional. The United States Supreme Court held the bonds to be valid obligations of the city through the operations of the act legalizing them, sustaining its constitutionality.[1]

for the purpose of ascertaining whether the mayor had been duly authorized to issue the bonds; that it is within the power of the mayor to pass upon that fact, and the issuance of the bonds by him is conclusive that the power existed. To this the judge said: "I cannot give my assent to this proposition, nor do any of the cases cited by the diligent counsel go to that extent. The decisions of United States Circuit Court of Appeals for the eighth circuit are conclusive on this court, and National Bank of Commerce *v.* Town of Granada, 10 U. S. App. 692; 4 C. C. A. 212; 54 Fed. Rep. 100, is decisive of this case. In that case the court says: 'The plaintiff was bound to know, independently of the recitals in the bond, that there was such an ordinance in existence. If the officers authorized to issue the bonds upon a condition are not the appointed tribunal to decide the fact which constitutes the condition, their recital will not be accepted as a substitute for proof. The very ground of the estoppel is that the recitals are the official statement of those to whom the law refers the public for authentic information on the subject.'"

[1] Read *v.* Plattsmouth, (1882) 107 U. S. 568. Mr. Justice MATTHEWS, speaking for the court, said: "The act in question, so far as it relates to the bonds in suit, does not confer any corporate power upon the city in the sense of the Constitution of the state. The statute operates upon the transaction itself, which had already previously been consummated, and seeks to give it a character different in its legal aspect from that which it had when it was *in fieri*. Whether such an effect may be given by a legitimate exercise of legislative power, depends upon those considerations which draw the line beyond which retroactive laws cannot pass, and is not affected by the supposed form of the contract as a special or general act conferring corporate power. For it operates upon the rights of the parties as determined by the equity of their circumstances and relations, and gives to them the sanction derived from subsequent confirmation by clothing them with powers which are essential to their enforcement but not to their existence. Within the usual limitations prescribed by our written Constitutions, such as have been quoted from that of Ne-

§ 415. **Bonds for public improvements — limitations on power to issue.**— As to the power of a city of Texas, the Constitution of which state contains a provision that no city shall ever incur a debt for any purpose, or in any manner, unless at the same time provision is made for levying and collecting a tax sufficient to pay the interest, and a sinking fund of at least two per cent per annum, and another that the tax to be levied for the erection of public buildings and other permanent improvements shall not exceed twenty-five cents of the $100 in any one year, has been considered by the United States Circuit Court of Appeals for the fifth circuit in an action against it upon bonds issued for public improvements. The court held that the power to create debts for this purpose was limited to a sum, upon which the interest, together with two per cent for the sinking fund would not exceed the revenue derived from a tax of twenty-five cents on the $100. After this city had issued bonds to such an amount that the interest and sinking fund absorbed the whole of the tax of twenty-five cents upon the $100, there was issued another series, and it was provided that the interest and sinking fund for this second series should be appropriated out of the general revenue of the city. The first issue of bonds, to the full amount authorized by the Constitution of the state, the court held, exhausted the power of the city to contract debts of this kind, and the additional series of bonds was held to be void, without regard to the authority of the city to apply its general revenue to the payment of interest and sinking fund of a bonded debt.[1]

braska, this may be done, provided it can be done without the destruction of rights recognized by the law as vested. In the present case the statute in question does not impose upon the [defendant city], by an arbitrary act, a burden without consent and consideration. On the contrary, upon the supposition that the bonds issued, as to the excess over fifteen thousand dollars, were void, because unauthorized, the city * * * received the money of the plaintiff in error, and applied it to the purpose intended, of building a school house on property, the title to which is confirmed to it by the very statute now claimed to be unconstitutional, and an obligation to restore the value thus received, kept and used, immediately arose. This obligation, according to general principles of law accepted in Nebraska, was capable of judicial enforcement. Clark *v.* Saline County, 9 Neb. 516; Louisiana *v.* Wood, 102 U. S. 294; New Orleans *v.* Clark, 95 U. S. 644; Hitchcock *v.* Galveston, 96 U. S. 341; Parkersburg *v.* Brown, 106 U. S. 487; Chapman *v.* Douglas, 107 U. S. 348."

[1] Millsaps *v.* City of Terrell, (1894) 60 Fed. Rep. 193.

§ 416. Effect of an order by resolution of council of a city for an election to authorize the issue of bonds.— A city of Kansas having issued its bonds upon which this action was founded under the general law of that state declaring that cities may "borrow money and issue bonds therefor" whenever "the city council shall be instructed so to do" by vote of the inhabitants the United States Circuit Court of Appeals for the eighth circuit held it to be no objection to the validity of the bonds that the council submitted the matter to the electors by means of a resolution, rather than an ordinance, there being nothing in the statutes expressly requiring an ordinance in such case.[1]

[1] City of Alma *v.* Guaranty Savings Bank, (1894) 60 Fed. Rep. 203. THAYER, D. J., speaking for the court, said, *arguendo:* "The law is well settled that a municipal corporation may declare its will as to matters within the scope of its corporate powers, either by a resolution or an ordinance, unless its charter requires it to act by ordinance; and generally it is of little significance whether a legislative measure is couched in the language of an ordinance or of a resolution, where it is enacted with the same formalities which usually attend the adoption of ordinances. If the action taken by a municipality amounts to prescribing a permanent rule of conduct, which is to be thereafter observed by the inhabitants of the municipality, or by its officers in the transaction of the corporate business, then, no doubt, the rule prescribed may be more properly expressed in the form of an ordinance; but it is eminently proper to act by resolution if the action taken is merely declaratory of the will of the corporation in a given matter, and is in the nature of a ministerial act. Beach Pub. Corp. § 484, and cases there cited; City of Lincoln *v.* Sun Vapor Street-Light Co., 59 Fed. Rep. 756. In the present case the resolutions in question appear to have been passed and entered at large upon the journal of the council, in the same manner that the council record also discloses that the vote was taken by yeas and nays, and that the resolution of March 18, 1889, directing an election to be held was published in substantial compliance with the provisions of the charter touching the publication of ordinances, and that after the council had been instructed by the inhabitants of the city to issue the bonds, at an election held for that purpose, the council did not publish its final resolution to issue the bonds, which had been passed in obedience to the popular mandate. It is also noteworthy that all of the proceedings taken to secure the issue of the bonds were conducted with the greatest publicity and apparent fairness. It is not charged that the resolutions were rushed through the council secretly, or with indecent haste, or that any one has been defrauded, or that the city did not receive full value for its bonds. Moreover, it is apparent, from an inspection of the first resolution, that, before the council took any action, the project of issuing the bonds had been discussed at a public meeting of the inhabitants of the city, and that the council had been requested to order an election." The court distinguished National Bank of Commerce *v.* Town of Granada, 54 Fed. Rep. 100; s. c., 4 C. C. A. 212; 10 U. S. App. 692.

§ 417. **Bonds valid when issued as a part of the general indebtedness of the city.**— In an action by citizens to restrain the issuing by a Minnesota city of certain "water and light bonds" it was contended by those bringing the action that it was the purpose of the legislature, in its amendment to the charter of the city, manifested by the wording of the law, to make the water and light bonds a special indebtedness, not enforceable against the city as were other bonds, but solely and exclusively by resort to the water and light franchises, structures and appliances. The Supreme Court of that state, however, affirmed the order of the court below sustaining a demurrer to the complaint, holding that under the amendment such bonds might be issued by the authorities of the city, the requisite preliminaries having been observed, as a part of the general indebtedness of the city, notwithstanding such bonded indebtedness already exceeded five per cent of the assessed valuation of the taxable property in the city, according to their then last assessment.[1]

[1] Woodbridge *v.* City of Duluth, (Minn. 1894) 59 N. W. Rep. 296. The court said: "It seems to be claimed that, because these bonds were made a special and exclusive lien upon the water and light plant or plants, it inevitably follows, without regard to other language found in the law, that they cannot be a part of the general indebtedness of the city, or, if they are, that they fall within the inhibitory clause of the charter. It would be a forced and unnatural construction of the enactment, probably operating to wholly defeat its purpose, to hold that the holders of the bonds could only look to the franchises, structures and appliances for payment. We are not inclined to presume that the legislature simply intended to confer upon the city the worthless privilege of putting bonds on the market, in the hope of their being purchased by capitalists who would be willing to advance money, that the city, without incurring any liability itself, might experiment in furnishing water and light to its citizens. Not only this, but if these bonds were not to be considered as a part of the general indebtedness of the city all reference to the five per cent clause was superfluous and unnecessary. There can be no doubt but that, while these bonds, undoubtedly for better security, are made a special and exclusive lien upon the plants, they were a part of the bonded indebtedness of the city as much as any other bonds. This leads up to the important inquiry already stated, and we are of the opinion that there is no ambiguity or doubt about the legislative intent and purpose, as expressed in the amendment. It will be noticed, and we have already referred to this, that by the first paragraph of the amendment to section 9 the council was authorized to make temporary loans, issuing coupon notes therefor, and, that there might be no question as to these notes, it was expressly provided that the indebtedness incurred in this way should be taken and held as part of the total indebtedness referred to in a preceding and prohibitory clause of the section. Then comes that part of the amendment which covers and authorizes the issu-

§ 418. Validity of bonds as affected by a restriction in the charter of a city.— A section of the charter of a city in Indiana provided for making "original loans" on the part of the city with this limitation: "Such loans may be made only for the purpose of procuring money to be used in the legitimate exercise of the corporate powers of such city and for the payment of legitimate corporate debts." The validity of certain bonds which had been issued by the city as part of a series of bonds for which the city had received bids was in question in an action in the federal court for that district, brought by the bidders for their relief from the bid and a recovery of money they had deposited as an earnest of their good faith. These bonds were for an amount to cover the amount of certain bonds of the city previously issued in payment for a farm, and which had been paid out of the treasury of the city and extinguished, the intention of their issue being with the proceeds to replace that money. The court held that as original loans these bonds were void and beyond the power of the city to issue.[1]

ance of the bonds in question, and again did the legislature express itself in plain language, by declaring that the bonds so issued should not be deemed a part of the general indebtedness already referred to as not to exceed five per cent of the assessed valuation. Putting the language in a different form, it is that in estimating the bonded indebtedness of the city, for the purpose of ascertaining whether the limit had been reached, the water and light bonds should not be taken into consideration. No other effect can be given the language, and if it does not mean this it means nothing at all. The entire structure of the amendment indicates, unmistakably, that it was well appreciated by the legislature that water and light bonds which would serve the purposes of the city, and enable it to buy or build the necessary experiment, would have to be issued in a large amount far exceeding that already authorized. The office of the amendatory legislation was to empower the city to proceed without limitation or restriction as to the amount of the issuance of the bonds for the particularly specified object."

[1] Coffin *v.* City of Indianapolis, (1894) 59 Fed. Rep. 221. BAKER, D. J., said: "This limitation [in the charter] evidently means that when the city proposes to borrow money the ordinance shall state the purpose of the loan, in order that it may appear that the money procured is to be used in the legitimate exercise of corporate powers, or for the payment of legitimate corporate debts. If the city may issue and sell its bonds to raise money without stating any lawful purpose for which the money is to be used, the bonds would be valid if the money was used for a legitimate corporate purpose, and invalid if the money was illegitimately used. Such a construction would place upon the purchaser of bonds the burden of seeing to the rightful application of the money if he would maintain their validity. The city, in the present case, has rightfully

recognized the necessity of stating the purpose of the issue and sale of the bonds. Is the purpose stated as to twenty-one thousand dollars of the bonds a legitimate one? As we have already said, these bonds were not to be issued and sold for the payment of a legitimate corporate debt, because there was no debt to be paid. The Sellers farm debt had been paid, and the bonds evidencing the same had been canceled and discharged. Thereafter the debt ceased to exist. Is the raising of money, the issue and sale of bonds for the purpose of putting back into the treasury a sum equal to what had been used in the payment of a debt of the city 'a legitimate exercise of the corporate powers of such city?' If the city may issue and sell its bonds to replace in the treasury the money paid out on account of the Sellers farm debt, it may issue and sell its bonds to replace in the treasury all the moneys ever paid out by it on account of its debts and liabilities. In my judgment the issuance and sale of bonds for such a purpose is not within the scope of its legitimate corporate powers. The city cannot issue or sell its original bonds except for the purpose of raising money to pay some legitimate debt or liability, or to meet some future liability or obligations incurred, or to be incurred, in the legitimate exercise of its corporate powers." In the same opinion, in another place, it was said: "It is the settled law of Indiana that a city organized under the laws of the state cannot issue and sell its bonds, to raise money by way of loan, unless expressly authorized so to do. City of Aurora *v.* West, 22 Ind. 88; State *v.* Hauser, 63 Ind. 155; Rushville Gas Co. *v.* City of Rushville, 121 Ind. 206; s. c., 23 N. E. Rep. 72. Such is also the settled doctrine of the Supreme Court of the United States. Brenham *v.* Bank, 144 U. S. 173; s. c., 12 Sup. Ct. Rep. 559. And in case of doubt touching the existence of the power on the part of a city to issue and sell its bonds to raise money by way of loan, such doubt must be resolved against the existence of the power."

CHAPTER XX.

TOWNSHIP BONDS.

§ 419. Effect of ordinance of town council not being published upon the validity of the bonds.
420. Bonds for purchase of gravel road under Indiana statute — statute held to be constitutional.
421. The duty and power of county authorities where the vote of the towns is favorable in such cases.
422. Effect upon bonds of a constitutional limitation upon the indebtedness to be incurred by towns.
§ 423. Town bonds for improvement of public park under resolution of the Connecticut legislature — when authorized and to what extent.
424. The effect of recitals in town bonds as to estoppel of the town to claim they were issued without authority.
425. What is required of a bona fide purchaser.

§ 419. Effect of ordinance not being published upon the validity of bonds.— A town of Colorado issued certain fifteen-year bonds to a contractor for building a reservoir for water purposes under circumstances which indicated fraudulent collusion between him and the town authorities. Some of these bonds passed in regular course of trade to a bank which brought an action upon coupons for interest thereon in the federal court for that district. The question decided was between the bank, a purchaser of the bonds for valuable consideration, before maturity, and in good faith, and the defendant corporation, the officers and agents of which permitted the bonds to be placed upon the market as commercial paper. The bonds as offered for sale were in due form and properly executed. They had been registered with the state auditor and recorded by the town treasurer, as certified on their face. It was recited in the bonds that they had been issued under the sanction of an ordinance providing therefor, for funding and paying the existing debts of the city of Grenada. The United States Circuit Court held that it was open to the town to defend in this action even against the *bona fide* holder and purchaser for value, notwithstanding the recital in the bonds; that there was no authority for the issue of the bonds, and they were

invalid obligations even in the hands of the holder suing upon them.[1] In the United States Circuit Court for the district, by the court, upon an agreed statement of facts upon the new trial which had been ordered, in the same case, the judgment was similar to that in the District Court.[2] This judgment was appealed from,

[1] National Bank of Commerce *v.* Town of Granada, (1890) 44 Fed. Rep. 262.

[2] National Bank of Commerce *v.* Town of Granada, (1891) 48 Fed. Rep. 278. PARKER, J., in rendering his judgment finding the bonds to be invalid, said: "It is my conclusion that under the laws of Colorado there must have been an ordinance of the town of Grenada to authorize the issuance of the bonds, the coupons of which are the basis of the suit in this case." He then quoted the general statute of the state as to ordinances of municipal corporations, and said: "By the terms of this section of the statute law of the state, when the same is given a reasonable construction, all by-laws of a general or permanent nature must be published as required by the above-named section. This ordinance of the town of Grenada passed by its council, purporting to authorize the issue of the bonds to which the coupons in suit were attached, is of a general or permanent nature, and all by-laws or ordinances of a general or permanent nature do not take effect or be in force until the expiration of five days after they have been published or posted. It appears from the agreed statement of facts in this case that there never was any publication of the ordinance in a newspaper, or in any manner or form whatever. The statute requiring the publication of the ordinance is mandatory, and the ordinance, without the requisite publication, is a nullity, and consequently of no force or validity. There is, then, no authority for the issue of the bonds to which the coupons in suit belong. The recital in the bond, that it was issued under an ordinance of the city of Grenada passed by the council of said city, will not make the bond valid in the hands of plaintiff as an innocent holder, if it, under the law, was bound to take notice of the legal authority of the town of Grenada to issue the bond. The legal authority of the officers of the town must be found in some ordinance authorizing them to act. The recitation on the face of the bond that it was issued under an ordinance referred the purchaser to the law requiring the publication of the ordinance. The ordinance conferred no legal authority upon the town officers to execute and issue the bonds until the expiration of five days after it had been published. The corporation of Grenada must have had legislative authority to issue the bonds issued by it. Although the plaintiff is a holder for value and before maturity, it must, at its peril, take notice of the existence and terms of the law by which it is claimed the power to issue such bonds is conferred. The holder of a municipal bond is chargeable with notice of the statutory provisions under which it was issued." The court cited in support of the last point Bank *v.* City of St. Joseph, 31 Fed. Rep. 216; Anthony *v.* Jasper County, 101 U. S. 693; Ogden *v.* Daviess County, 102 U. S. 634; Bank *v.* Porter Township, 110 U. S. 608; s. c., 4 Sup. Ct. Rep. 254; McClure *v.* Township of Oxford, 94 U. S. 429. This last case was regarded by the court as especially relevant to the present one.

and the United States Circuit Court of Appeals affirmed the judgments already rendered in the courts below.[1]

§ 420. Bonds for purchase of gravel road under Indiana statute — statute held to be constitutional.—The statute of Indiana which provides for the purchase of gravel roads upon an

[1] National Bank of Commerce *v.* Town of Granada, (1893) 54 Fed. Rep. 100. As to the questions involved and the views of this court upon them, CALDWELL, Circuit Judge, said: "We think the principal and vital question in this case is whether the powers conferred on the board of trustees may be exercised without an ordinance containing the usual and necessary provisions to guide, control and bind the town and its officers and the public in the execution of the funding scheme, and to protect all persons in their rights acquired thereunder. We entertain no doubt but that the appropriate mode for the town to proceed under the act in question is by ordinance of its board of trustees. The proceeding involves the appointment and holding of an election, and the conversion of a non-negotiable floating debt into the form of negotiable bonds drawing a high rate of interest payable semi-annually, and which must run five, and may run fifteen, years. A measure requiring an expression of opinion from the voters of the town at the ballot box and involving such large values and of so much interest to the taxpayers of the town and the holders of its securities through so many years, ought not to be carried into effect except by the most solemn and deliberate mode of proceeding known to the law for giving expression to the corporate will. That mode is by ordinance. * * * The statutes of the state [of Colorado] which authorize the issue of refunding bonds, * * * the creation of new indebtedness, * * * and the appropriation of aid to public libraries, * * * require in terms that the same shall be done by ordinances. We think the board of trustees of the town had a correct conception of the proper mode of proceeding when they passed the ordinance in question." The statute prescribing the regulations as to ordinances is then referred to, and then the court resumed: "It is admitted that the ordinance in question was not 'recorded in the book kept for that purpose,' and was not 'authenticated by the signature of the presiding officer of the * * * board of trustees and the clerk,' and 'was never published in any paper or in any form or manner whatever.' It is obvious to our minds that the ordinance in this case was of a 'general or permanent nature' [the words of the statute], and as such could 'not take effect and be in force until the expiration of five days' after its publication. It provided for an election, and, therefore, concerned every legal voter of the town. It affected every taxpayer, whether a voter or not. It affected the creditors of the town, present and future. It involved the making and execution of contracts, and various other matters relating to funding the floating indebtedness of the town. If such an ordinance is not of a 'general or permanent nature' it would be extremely difficult to suggest one that is. The provision of the act, that such ordinances shall not take effect or be in force until they are published in the mode provided by the act, is mandatory. The ordinance, never having been pub-

election of the voters of the township or townships through which they pass, ordered upon petition of a certain number of the freeholders thereof, and the finding of certain facts as to the number of voters, etc., by the board of county commissioners, the purchase money to be provided by the issuing of county bonds of a certain kind, which are to be paid by a levy of taxes annually upon the property of the citizens of such townships, was attacked as unconstitutional in an action by taxpayers of one

lished, never went into effect. Not being in force, it conferred no authority on the board of trustees, or any officer of the town, to do any act under it; and no one could acquire any right based on it, or on any act of the officers of the town assuming to act under it. It had no more legal effect than if it had never been passed by the board of trustees. 1 Dill. Mun. Corp. §§ 331–334, and notes. But the learned counsel for the plaintiff in error contends that the recital in the bonds, that they 'are issued under an ordinance' of the town relieves the plaintiff from the burden of showing that the ordinance was published, and estops the defendant from showing that it was not. It has never yet been held that a false recital in a bond can make that a law which never was a law. When an ordinance has been duly enacted, and has taken effect, authorizing the officers of a town to issue its negotiable bonds upon certain precedent requirements or conditions, such as a petition of a given number of taxpayers, or a majority vote or other like conditions, and the officers issuing the bonds are the appointed tribunal to decide whether there has been a compliance with such precedent conditions, and the bonds issued recite that they are issued in pursuance of such ordinance, it is probably true that such recital, in favor of *bona fide* purchasers for value, would import a full compliance with the requirements of the ordinance, and preclude inquiry as to whether the precedent conditions were performed before the bonds were issued. But that doctrine has no application to this case. Here there was no ordinance in force under which the board of trustees, or any officer of the town, could perform any act. The authority to issue the bonds never attached, on any terms or conditions. The action of the mayor and clerk was not simply irregular, but was without the sanction of any law. The point was never reached at which they could lawfully do any act under the supposed ordinance. It is a case of a total want of authority to do the act upon any conditions, and not a case where the authority to do the act existed, but the conditions precedent to the exercise of the authority were not observed. The statute which provides that ordinances shall not take effect until they are published is a public statute, of which all persons are bound to take notice. The statute makes the recording of an ordinance in the ordinance book *prima facie* evidence that it has been published according to law. But this ordinance was not recorded, nor authenticated as an ordinance by the signatures of the mayor and clerk, as required by law. Moreover, it is not shown that the mayor and clerk, or either of them, had any duty or function to perform in relation to publishing ordinances, or determining when they had been published according to law. The determination of this fact,

of three townships upon the property of which such a levy of taxes was made, to restrain the collection of such tax. The contention on behalf of the taxpayers was that the statute was void as violative of these constitutional provisions, to wit: "The general assembly shall not pass local or special laws in any of the following enumerated cases, that is to say: For the assessment and collection of taxes for state, county, township or road purposes;" also, the following: "The general assembly shall provide, by law, for a uniform and equal rate of assessment and taxation, and shall prescribe such regulations as shall secure a just valuation for taxation of all property, both real and personal, excepting such only for municipal, educational, literary, scientific, religious or charitable purposes, as may be specially exempted by law. The Supreme Court of the state upheld the statute as constitutional.[1]

when it becomes material, and is contested, and the ordinance has not been recorded, is, under the statute, a matter for judicial inquiry. The statute itself provides that it shall be a sufficient defense to any suit or prosecution for a fine, penalty or forfeiture to show that the ordinance imposing it was not published as required by the statute, and it is obvious that the same defense must prevail against any civil right grounded upon an ordinance which was never published, no matter by or against whom such right is asserted. The plaintiff was bound to know, independently of the recital in the bond, that there was such an ordinance in existence. This fact once established, it might well assume that the recital was sufficient evidence that the conditions prescribed by the ordinance for issuing the bonds had been complied with. It was as much the right and duty of the plaintiff to determine this question as it was the clerk and themayor, and the determination of either, in any form, would not bind or conclude the town. It is only when officers are invested by law with the authority to determine or adjudicate upon the fact that their recital operates as an estoppel. If the recital in this case had stated, in terms, that the ordinance had been duly published, it could not have estopped the town, because neither the mayor nor the clerk, nor both together, are invested with the authority to determine that question, and anything they might say or certify to on the subject, save as witnesses in court, would not be evidence anywhere, or bind any one. Dixon Co. *v.* Field, 111 U. S. 83, 94; s. c., 4 Sup. Ct. Rep. 315; Sutliff *v.* Lake County Commis., (1892) 13 Sup. Ct. Rep. 318. * * * The law does not refer the public to these officers, or to either of them, for information as to the publication of town ordinances; and their statements upon that subject have no more significance or binding force than those of any other citizen of the town."

[1] Gilson *v.* Board of Commissioners of Rush County, (1891) 128 Ind. 65. *Arguendo*, the court said, upon the point made as to the first quoted section: "It is held that a statute which is of general and uniform operation throughout the state, and operates alike upon all persons, under the same circumstances, is not subject to the

§ 421. The duty and power of county authorities where the vote of the towns is favorable in such cases.—The court, in construing the statute of Indiana as to purchase of a gravel road running through several townships, held that when the election is held in a number of townships, it hav-

objection that it is special or local legislation. State ex rel. *v.* Reitz, 62 Ind. 159; McLaughlin *v.* Citizens', etc., Assn., 62 Ind. 264; Heanley *v.* State, 74 Ind. 99; Elder *v.* State, 96 Ind. 162. The statute we are now considering is of uniform operation throughout the state of Indiana, and applies alike to all persons coming within its operation, and is not in conflict with the provisions of [the first section quoted]." Whether it was in conflict with the last section quoted, the court considered a more serious question and fully discussed it, as follows: "This provision of our Constitution received a construction in the case of Bright *v.* McCullough, 27 Ind. 223. It was said in that case: 'The section does not require that the rate of assessment shall be uniform and equal for all purposes throughout the state, and we think its meaning clearly is that the rate of assessment and taxation must be uniform and equal throughout the locality in which the tax is levied.' So, again, it received a construction in the case of LaFayette, etc., R. R. Co. *v.* Geiger, 34 Ind. 185. That was a suit to enjoin the levy and collection of a tax in aid of the construction of a railroad. It was contended that inasmuch as the railroad ran through the counties of Madison, Tipton, Clinton, Tippecanoe and Benton in this state, it was necessary that each and all of the counties must vote for an appropriation and assess the same amount of tax in each county to make it uniform and equal. In answer to this contention, the court said: 'If the tax assessed is equal and uniform in the county where assessed, it will be in strict accordance with the requirements of the Constitution.' See, also, John *v.* Cincinnati, etc., R. R. Co., 35 Ind. 539. It is not unusual for the legislatures of the several states in the Union, in the exercise of the general power of taxation, as well as in the power of local assessments, to create a special taxing district without regard to municipal or political subdivisions of the states, and to levy a tax on all property within such district by a uniform rule, according to its value, for the purpose of aiding in the construction of public improvements. Our laws providing for street improvements, for the construction of free gravel roads, for the construction of ditches and drains, and for aid in the construction of railroads, are examples of this kind of legislation. True, in most cases, such improvements are paid for by local assessments against real property, which, in theory, is benefited to an amount equal to the assessment. But it is by no means universally true that such improvements are paid for by assessments against real estate supposed to be benefited; but, on the contrary, they are often paid for by the assessment of a tax on all property found within the taxing district. The doctrine announced in Bright *v.* McCullough, *supra*, that the requirements of [the last section of the Constitution referred to] are fulfilled when the rate of assessment and taxation is uniform and equal throughout the taxing locality, has often been affirmed by this court. Palmer *v.* Stumph, 29 Ind. 329; Anderson *v.* Kerns Draining Co., 14 Ind. 199; Goodrich *v.* Winchester, etc., T. P. Co., 26 Ind. 119. In the case of Bowles *v.* State, 37 Ohio St. 35, the question now under consideration was

ing been ordered in response to the petition signed by voters of all the townships, and the majority of the voters is in favor of making the purchase of the gravel road running through the townships, with a view to its becoming a free gravel road, it becomes the duty of the county commissioners of the county in which the townships are situated to make the purchase. And they then are authorized to issue bonds for the purpose and levy a tax upon the citizens of the townships interested for their payment.[1] The Supreme Court of the United States has held that the requirement of a charter, that the bonds issued by a municipal cor-

discussed at some length by the Ohio court. The case involved the constitutionality of a statute passed by the general assembly of that state authorizing the assessment of all property, both real and personal, within a given district, to pay for the construction of a free turnpike road. It was contended that the legislature had no power to create a taxing district without regard to the boundaries of the political or municipal subdivisions of the state, and in answer to this objection the court said: 'That the power is not expressly inhibited is clear, and we are persuaded there is no implication against it from the fact that it has always been exercised without challenge in divers ways for the purpose of promoting local advantages, not only in the exercise of the power of local assessments, where the burden of local improvements has been placed upon property specially benefited and in proportion to the benefit, but by general taxation upon local districts other than municipal or political subdivisions Notably, special taxing districts have been created for the purpose of supporting and maintaining schools and highways by the subdivisions of townships; and we can see no difference in principle between such legislation and the statute under consideration.' These several adjudications seem to be in exact accord with the elementary books upon the same subject. Cooley Taxation (ed. 1876), p. 113; see, also, pp. 110, 111, 112; Elliott Roads & Streets, 392, 393." See, also, to the same effect, People *v.* Central Pacific R. R. Co., 43 Cal. 398; County Judge *v.* Shelby R. R. Co., 5 Bush, 225; Challiss *v.* Parker, 11 Kans. 394; People ex rel. *v.* Draper, 15 N. Y. 532; Buffalo, etc., R. R. Co. *v.* Board, etc., 48 N. Y. 93; Litchfield *v.* McComber, 42 Barb. 288; Sangamon, etc., R. R. Co. *v.* County of Morgan, 14 Ill. 163; Bakewell *v.* Police Jury, 20 La. Ann. 334; Inhabitants of Norwich *v.* County Commissioners, 13 Pick. 60; Inhabitants of Brighton *v.* Wilkinson, 2 Allen, 27; Salem Turnpike *v.* County of Essex, 100 Mass. 282; Missouri River, etc., R. R. Co. *v.* Morris, 7 Kans. 210.

[1] Gilson *v.* Board of Comrs. of Rush County, (1891) 128 Ind. 65. The court said: "In our opinion, it was the intention of the legislature, in passing the act under consideration, that where two or more townships joined in a petition to the board of county commissioners to purchase a particular toll-road, all the townships joining in such petition should be taxed to pay for the same, in the event a majority of the votes cast was in favor of such purchase, though there may have been a failure to obtain a majority in one of the townships. Where the townships

poration shall specify for what purpose they are issued, was not so far satisfied by a bond which purported on its face to be issued by virtue of an ordinance, the date of which was given, but not its title or contents, as to cut off defenses which might otherwise be made.[1]

have joined in such petition, and the vote is in favor of the purchase, the townships thus voting may well be said to have voted in favor of such purchase. The result of holding otherwise might be that two townships would purchase the two ends of a toll-road while a majority of one vote in a township between the two would defeat the purchase of the center, and thus destroy the value of the road as a free thoroughfare. We do not think it was the intention of the legislature to permit such a result. The contention that the elections, in all cases under this law, are to be several, is destroyed by the provision made for a joint petition. Had it been the intention of the legislature that the purchase should depend on the result of the election in each township, it is reasonable to assume that the legislature would have provided for several elections, and would have made no provision for joint petitions and a joint election."

[1] Barnett *v.* Denison, (1892) 145 U. S. 135. The state of the law in such a case was declared by Mr. Justice Brown, speaking for the court, to be as follows: "It is the settled doctrine of this court that municipal corporations are merely agents of the state government for local purposes, and possess only such powers as are expressly given, or implied, because essential to carry into effect such as are expressly granted (1 Dill. Mun. Corp. § 89; Ottawa *v.* Carey, 108 U. S. 110); that the bonds of such corporations are void unless there be express or implied authority to issue them (Wells *v.* Supervisors, 102 U. S. 625; Claiborne County *v.* Brooks, 111 U. S. 400; Concord *v.* Robinson, 121 U. S. 165; Kelley *v.* Milan, 127 U. S. 139); that the provisions of the statute authorizing them must be strictly pursued, and that the purchaser or holder of such bonds is chargeable with notice of the requirements of the law under which they are issued. Ogden *v.* County of Daviess, 102 U. S. 634; Marsh *v.* Fulton County, 10 Wall. 676; South Ottawa *v.* Perkins, 94 U. S. 260; Northern Bank *v.* Porter Township, 110 U.S. 608; Hayes *v.* Holly Springs, 114 U. S. 120; Merchants' Bank *v.* Bergen County, 115 U. S. 384; Harshman *v.* Knox County, 122 U. S. 306; Coler *v.* Cleburne, 131 U. S. 162; Lake County *v.* Graham, 130 U. S. 674. It is certainly a very reasonable requirement that the bonds issued shall express upon their face the purpose for which they were issued. In any event, it was a requirement of which the purchaser was bound to take notice, and if it appeared upon their face that they were issued for an illegal purpose they would be void. If they were issued without any purpose appearing at all upon their face, the purchaser took the risk of their being issued for an illegal purpose, and if that proved to be the case they are as void in his hands as if he had received them with express notice of their illegality. Ordinarily the recital of the fact that the bonds were issued in pursuance of a certain ordinance, would be notice that they were issued for a purpose specified in such ordinance (Hackett *v.* Ottawa, 99 U. S. 86), and the city would be estopped to show the fact to be otherwise. Ottawa *v.* National Bank, 105 U. S. 342. But where the statute re-

§ 422. **Effect upon bonds of a constitutional restriction upon the indebtedness to be incurred by towns.**— The board of trustees of a town in Indiana adopted an ordinance directing that bonds of the town be issued to procure funds with which to rebuild a school house which had been destroyed by fire. The Supreme Court of that state held that such proposed bonds were within the constitutional provision of that state restricting the power of public corporations to incur indebtedness, which is in these words: "No political or municipal corporation in this state shall ever become indebted, in any manner or for any purpose, to an amount in the aggregate exceeding two per centum on the

quires such purpose to be stated upon the face of the bonds, it is no answer to say that the ordinance authorized them for a legal purpose. if in fact they were issued without consideration and for a different purpose. In this case the bonds were not only issued for a purpose not named in the ordinance, viz., in aid of the Texas and Atlantic Refrigerator Car Company, which had agreed to erect at Denison slaughter houses, tanks, machinery and other material of the value of fifteen thousand dollars, but upon a consideration which had wholly failed, the company having failed to comply with the terms of the contract; and the bonds, so far as they were known to exist, were canceled." The court then commented upon certain cases to which their attention had been called in these words: "In Kansas *v.* School District No. 3, 34 Kans. 237, relied upon by the plaintiff, the state sued a school district upon certain school-district bonds and their coupons. Upon the trial the defendant objected to the introduction of any evidence upon the petition, upon the ground that the same did not state facts sufficient to constitute a cause of action, and the court sustained the objection and dismissed the action. One of the objections urged by the defendant against the petition was that the bonds did not state, as required by statute, the purpose for which they were issued. The court held that the bonds were not void for that reason, because under the allegations of the petition they must be considered as issued in good faith; 'that the school district received ample consideration for them, and that the state of Kansas is an innocent and *bona fide* purchaser of them, for nothing appears to the contrary in the petition, and all the allegations of the petition would tend to indicate this.' This ruling, however, is not inconsistent with the idea that if they had been issued for an illegal purpose the purchaser would have been chargeable with notice of such illegality by reason of the omission to state on the face of the bonds the purpose for which they were issued. In Young *v.* Camden County, 19 Mo. 309, the act required that county warrants should be written or printed in Roman letters without ornament, in order to prevent the issuing of paper by County Courts which could be used as a circulating medium. This was held to be merely directory; but this case, though cited by the plaintiff here, is not in point. The court held expressly that all the words prescribed by the statute were in the warrants, and that the introduction of other words did not vitiate them."

value of the taxable property within such corporation, to be ascertained by the last assessment for state and county taxes previous to the incurring of such indebtedness; and all bonds or obligations in excess of such amount given by such corporation shall be void." Also, that because there was a provision or promise to levy taxes to pay the bonds did not prevent the application of the constitutional provision to the bonds.[1] The court further sustained the right of a taxpayer to maintain an action for injunction to prevent the issue of these town bonds as without authority.[2]

§ 423. **Town bonds for improvement of public park under resolution of the Connecticut legislature — when authorized and to what extent.**— A Connecticut town was empowered by a resolution of the general assembly to issue its bonds to an amount not exceeding $200,000, to be used exclusively for the extension and improvement of the public park system of the town; the act to take effect when accepted at a special town meeting to be called by the selectmen; and the meeting to have power to take action with respect to the issuing of the bonds, and their form and terms. A later section provided that the park commission created by the act should not make any expenditure, or contract for any, exceeding the amount which shall have been previously appropriated by the

[1] Town of Winamac *v.* Huddleston, 1892) 132 Ind. 217.

[2] Ibid. It was said by the court: "There can be no doubt that if the bonds are executed as proposed, and are of any validity, they will create a debt against the public corporation. In this particular, as in others, this case is radically different from that of The City of Valparaiso *v.* Gardner, 97 Ind. 1. The debt created by a bond executed by a public corporation is not an obligation payable out of specific funds, but is a contract to pay money generally, and, hence, this case is not within the doctrine of such cases as Quill *v.* City of Indianapolis, 124 Ind. 292; Strieb *v.* Cox, 111 Ind. 299; Board, etc., *v.* Hill, 115 Ind. 316. A valid bond binds the corporation directly and unconditionally unless it is otherwise expressly stipulated in the instrument as provided by law. If the bonds to be issued are not valid because of want of authority, then, no matter what may be the cause of the invalidity, they should not be issued, so that if counsel are right in saying that the town has no authority to issue the bonds the judgment below must be sustained." As to the remedy in such a case it was said: "There is no other remedy of equal power and efficiency, and the case here comes within the rule declared in such cases as Watson *v.* Sutherland, 5 Wall. 74; Denny *v.* Denny, 113 Ind. 22; Bishop *v.* Moorman, 98 Ind. 1, and other cases there cited."

town for its use. At a meeting warned and held for the purpose the town accepted the resolution of the general assembly and voted "that the selectmen and treasurer are hereby directed to prepare suitable bonds as authorized by said act, not exceeding two hundred thousand dollars, of the tenor, character and terms hereinafter provided, and are authorized to dispose of them in such amounts and at such times as shall be required by the park commission, to provide the sums made necessary by said commission in its proceedings under said act." Parties from whom the park commissioners had purchased lands for a public park, with the proper officials of the town, agreed upon a submission to the Supreme Court of the question of the right and duty of the officials of the town to issue bonds in payment of the land so purchased. The court held that it was the duty of the selectmen and treasurer of the town to issue bonds within the limit prescribed, to an amount sufficient to pay for the lands.[1]

[1] Woodward *v.* Reynolds, (1890) 58 Conn. 486. *Arguendo*, it was said by the court: "At the meeting held in pursuance of [the] warning [above referred to]. in connection with a vote prescribing what the tenor, character and terms of the bonds should be, the following vote was passed: '*Voted*, that the selectmen and town treasurer be and are hereby directed to prepare and procure suitable engrossed bonds, as authorized by said act, not exceeding two hundred thousand dollars in total amount, bearing interest at a rate not exceeding three and a half per cent per annum, and of the tenor, character and terms hereinafter provided; and are further authorized to dispose of said bonds from time to time at not less than par and accrued interest, in such amounts and at such times as shall be required by the park commission to be constituted under the provisions of said act, in order to provide the sums made necessary by said commission in its proceedings under said act.' Whatever opinion may be held as to the effect of these votes, no question, so far as we know, has been or indeed can be raised as to the power conferred by the resolution, and the warning of the meeting contained a sufficient notice that the town would or might take the action indicated by the votes. The only question then is, whether these votes constitute an appropriation by the town within the meaning of section four of the resolution." Referring to definitions of "to appropriate" it is said: "In the case at bar, after the bonds are issued by the town, the resolution itself provides that they shall be used solely for the extension and improvement of the public park system in the manner provided in the resolution. This is in itself an appropriation of the bonds by legislative provision, but it is claimed that it is not the appropriation referred to in the fourth section of the resolution, and obviously it is not. Did the town then by the votes aforesaid make an appropriation within the meaning of section four? We think it did. Its agents, appointed for such purpose by the resolution itself, are directed and empowered by the town to procure

§ 424. **The effect of recitals in town bonds as to estoppel of the town to claim they were issued without authority.**—The recitals of those invested with the ministerial duty of issuing municipal bonds in such bonds, where there is an entire absence of power to issue them, will afford no protection to even *bona fide* holders for value, and the holders are bound to take notice of the want of authority to issue them.[1] The recitals in certain school bonds were that they were issued by the board of directors by authority of an election of the voters of the district in conformity with the provisions of the statute authorizing them. The United States Supreme Court held that it was not to be implied from these recitals that the bonds had been issued in conformity with the constitutional provision in regard to limit of indebtedness of such a corporation, and that, as to this defense, the holders took the bonds at their peril. In order to estop the municipality, in the name of which they have been issued, from showing that bonds were issued in violation of, or without authority of, law, the recitals on the face of the bonds should be clear and unambiguous.[2]

the bonds provided for in the resolution; the number and amount to be so procured and issued are specified; ample provision is made for their proper execution, authentication, and custody until they shall be issued and used; it is further provided that they shall be disposed of for the purposes of providing a fund for the use of the commission under the resolution; and, finally, these agents are fully empowered and directed to issue them from time to time as required for the needs of the commission. In this action of the town it is difficult to see what element or essential of a complete appropriation is wanting. There remained nothing more for the town to do. If the town had been called together prior to the purchase here in question, and after the passage of the votes, to make an appropriation with reference to the purchase of the land, it could only have instructed its agents to do what it had already empowered and directed them to do. The resolution itself provides in section six as follows: 'The bonds authorized in the first section of this act shall be prepared by the selectmen and town treasurer of New Haven, and shall be issued by them from time to time in such amounts as the park commission shall require. Such bonds shall in no case be sold or disposed of for less than par, and the avails of such as shall be issued shall be kept by the town treasurer as a special fund subject to the orders of the park commission, and shall be paid by him only on such orders.' Construing the votes in the light of this language of the resolution, we think they clearly make an appropriation, even within the meaning of section four of the resolution. To construe them otherwise would, we think, defeat the manifest intent and purpose of the town in passing them."

[1] Lippincott *v.* Town of Pana, 92 Ill. 24; Williams *v.* Town of Roberts, 88 Ill. 11.

[2] School District *v.* Stone, 106 U. S. 183. An illustration of bonds void by

§ 425. **What is required of a bona fide purchaser of bonds.** — The United States Supreme Court having ordered this case remanded upon its reversal of the judgment of the Circuit Court, upon the trial the Circuit Court made special findings sustaining the answers of the township and rendered judgment in its favor. The plaintiff's contention before the United States Circuit Court of Appeals for the sixth circuit was that, as it was a *bona fide* purchaser for value of the bonds in suit, it was not charged with notice of anything but the text of the statute itself, and was not bound to inquire into the motives or intent of the legislature, as inferred from other acts passed at the same time, and from facts extraneous to the act under which the bonds were issued, the existence or significance of which it could not know; that, on the face of the act, it raised exactly the same question of constitutionality which was considered in the case of Walker *v.* Cincinnati, 21 Ohio St. 14. The counsel for the plaintiff further attempted to explain away the decision of the Supreme Court of the United States by insisting that the hearing before that court [when it declared the act under which the bonds were issued to be unconstitutional] was on the averments of the answer with respect to the surrounding circumstances under which the bonds had been issued, and that no question was then before the court as to the right to use such evidence, in attacking the constitutionality of the law, against a *bona fide* purchaser of the bonds for value, without notice. To this the appellate court said: "We do not find it necessary to consider the objection that *bona fide* holders of bonds are not charged with a knowledge of surrounding circumstances which render the Enabling Act invalid, because while the Supreme Court did refer to such circumstances in the discussion of the act's validity, still the court held that, even if all the surrounding circumstances were ignored, the act was invalid, and was plainly distinguishable from the Walker case."[1]

reason of the notices of election in favor of them not being sufficient, and that no person could be an innocent purchaser of them. George *v.* Oxford Township, 16 Kans. 72. As to the unconstitutionality of an act of the Kansas legislature "authorizing townships to issue bonds for relief purposes," see State ex rel. *v.* Osawkee Township, 14 Kans. 418.

[1] Ætna Life Ins. Co. *v.* Pleasant Township, (1894) 62 Fed. Rep. 718, following Pleasant Township *v.* Ætna Life Ins. Co., 138 U. S. 67; s. c., 11 Sup. Ct. Rep. 215, holding the Enabling Act to be unconstitutional.

CHAPTER XXI.

SCHOOL DISTRICT BONDS.

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§ 426. **School district bonds generally.**— Municipal corporations, unless authorized by their charters, have no power to make and place in the market commercial paper, and persons dealing in municipal bonds issued by the officers of a school district must see that the power to issue them exists. There is no presumption that such paper has been issued within the scope of their power, as is the case with corporations created for business purposes.[1] Common councils of cities and boards of trustees of towns in Indiana are authorized to issue bonds of their municipalities, without petition of citizen owners of property therein, for the purpose of construction of school buildings.[2] Bonds issued and sold by a board of education for the purpose of building a dormitory and boarding house have been held to be illegal where such buildings were in no sense necessary for a public free school, and the power denied to levy taxes to pay interest on such bonds.[3] Bonds issued by a school district in excess of the consti-

[1] Hewitt *v.* Board of Education, 94 Ill. 528.

[2] Clark *v.* Town of Noblesville, 44 Ind. 83.

[3] Sherlock *v.* Winnetka, 68 Ill. 530.

tutional limit of the indebtedness of such a corporation have been held to be void even without regard to the good faith with which they were purchased and the want of notice of their invalidity.[1] School bonds, under the laws of Ohio, reciting upon their face conformity with the statute in the matter of their execution, have been held to be promissory notes negotiable by the law merchant.[2] Their qualities and incidents as commercial securities are not taken away by recitals on the face of the bonds that they were issued conformably to statute; neither is their negotiable character destroyed by the fact that option was reserved to the county to pay at any time before maturity.[3] The purchaser of a municipal bond issued without authority, or in violation of law, is not an innocent purchaser. The law makes it his duty to look to the authority under which the officers of the municipality acted. He may rely upon the recitals in the bonds for some purposes, but for proof of the authority of the officers of the corporation, such recitals are not binding on the principal where there is a want of authority.[4] If bonds purporting to be school bonds negotiable on their face be false and forged when delivered, the vendor of them, by the mere act of sale, will be held to impliedly warrant the genuineness of the bonds and liable to the vendee or his assignee for what the latter paid for them, with interest.[5] But a return or an offer to return the bonds is necessary to entitle the vendee to maintain a suit against the vendor for the amount he may have paid for such bonds.[6]

[1] Mosher *v.* Independent School District, 44 Iowa, 122. In Sherlock *v.* Winnetka, 68 Ill. 530, it was held that although the bonds issued in the case by a board of education, under a law for a proper purpose, may have been valid in the hands of innocent holders for value, notwithstanding a perversion of the uses for which they were intended, yet if a bill had been filed showing an intended perversion, or that the buildings to be erected with the proceeds of the bonds would be perverted, the board would have been enjoined from issuing them.

[2] Ackley School District *v.* Hall, 113 U. S. 135.

[3] Ibid.

[4] Town of Pana *v.* Lippincott, 2 Bradw. (Ill.) 466. An illustration of the estoppel of a municipal corporation by the recitals in a bond issued by it. Bolton *v.* Board of Education, 1 Bradw. (Ill.) 193. As to recitals in bonds not estopping the municipality to set up the defense of violation of the constitutional limitation upon its indebtedness in their issue, see Bates *v.* Independent School District, 25 Fed. Rep. 192; Geneva National Bank *v.* Independent School District, 25 Fed. Rep. 629; Nesbit *v.* Independent School District, 25 Fed. Rep. 635.

[5] Smith *v.* McNair, 19 Kans. 330.

[6] Ibid. Under the statute of California providing that trustees of a

§ 427. **Bonds executed by a de facto board of education.**—Where a *de facto* board of education, exercising all the powers and functions of such a corporation legally organized, is recognized and its action acquiesced in by the state and the citizens, bonds issued by it, within the powers granted to a board legally organized, are binding in the hands of *bona fide* purchasers.[1]

§ 428. **The power of a city in California to issue bonds for building school houses.**—In a controversy between a taxpayer and a city in California holding a freeholder's charter the power of the city to issue certain bonds for the purpose of building school houses was denied. There had been enacted by the legislature of California an act authorizing the incurring of indebtedness for municipal improvements, and issuing bonds therefor by cities, towns and municipal corporations. One provision of this act was that "Any city, town or municipal corporation, incorporated under the laws of this state, may, as hereafter provided, incur an indebtedness to pay the cost of any municipal improvement, or for any purpose whatever requiring an expenditure greater than the amount allowed for such improvement by the annual tax levy." The next provision in the act prescribed

school district may submit to the electors thereof the questions whether bonds shall be issued for purchasing a school lot and for building school houses, the Supreme Court held that the question of buying a lot and building a school house may be submitted jointly with the question of issuance of bonds. People ex rel. Hart, Atty.-Gen., *v.* Caruthers School Dist., (Cal. 1894) 36 Pac. Rep. 396. As to the holding of elections in the state of Washington for issuance of school bonds by school districts, and what is required by law, see Luzader *v.* Sargeant, (1892) 4 Wash. St. 299.

[1] National Life Ins. Co. of Montpelier *v.* Board of Education of City of Huron, (1894) 62 Fed. Rep. 788. The court said: "It is the province of the state to question, by proper judicial proceedings, [the] incorporation [of the board of education]; not that of a defendant in a private suit when it has asserted its corporate existence and incurred liabilities to innocent parties on the faith of it. When a municipal body has assumed, under color of authority, and exercised for any considerable period of time, with the consent of the state, the power of a public corporation, of a kind recognized by the organic law, neither the corporation nor any private party can, in private litigation, question the legality of its existence." Ashley *v.* Board, 60 Fed. Rep. 55, 63; s. c., 8 C. C. A. 455; County of Ralls *v.* Douglas, 105 U. S. 728, 730; Coler *v.* School Tp., (N. D.) 55 N. W. Rep. 587; Clement *v.* Everest, 29 Mich. 19; Burt *v.* Railroad Co., 31 Minn. 472; s. c., 18 N. W. Rep. 285, 289; People *v.* Maynard, 15 Mich. 463; Fractional School Dist. No. 1 *v.* Joint Board of School Inspectors, 27 Mich. 3.

the steps to be taken, a vote by the citizens, etc. All of the requirements of the statute had in the case of these bonds been complied with. It was claimed that the city had no power to issue its bonds for the construction of school houses, for the reason that the management of its schools was vested in a board of education, and that any bonds to be issued for school purposes must be authorized by that body. The Supreme Court of the state sustained the validity of these bonds.[1]

[1] In re Wetmore, (1893) 99 Cal. 146. *Arguendo*, it was said: "The provisions of the [statute quoted in the text] are general in their character, and give to every municipal corporation incorporated under the laws of this state the power to create a bonded indebtedness for any of the purposes authorized by the act. The indebtedness is not to be incurred, nor are the bonds to be issued, until after the voters of the municipality have so directed, but as it is the vote of the electors which determines that they shall be issued, it is immaterial to them what officers of the city carry out this vote. The act itself designates the legislative branch of the municipality as the body to determine in the first instance whether the public interest or necessity demands the construction or completion of the building or improvement, and also designates that body as the agency of the corporation through whose acts the indebtedness is to be created and evidenced. There is no particular mode provided by which the council shall ascertain this fact, but in a matter which pertains to the public schools the fact would naturally be ascertained by direct communication with the board of education, or by a request from that board, and inasmuch as that board has no power to issue the bonds of the city, it is but natural to assume that it would manifest its wishes to the council. The question, however, is not how the council shall ascertain whether the public interest demands the improvement, but whether it has any power to issue the bonds after it has so determined, irrespective of the mode of ascertaining it. Although the board of education has been intrusted with the management of the schools, and it is the body designated in the charter to build the school houses, there is nothing inconsistent with this provision for the legislature to designate the council as the body to give inception to the indebtedness and issue the bonds therefor. The power to build or improve the school houses which is vested in that board is distinct from the power to borrow money with which to build or improve them. The board of education, as such, is forbidden by the charter from incurring any indebtedness beyond the annual income for school purposes, and as the Constitution permits such indebtedness by any municipal corporation only after a vote of the electors therefor, it is competent for the legislature to designate the agent or body of the municipal government which shall act for it in carrying out the will of its electors, and for this purpose the legislative branch of that government would most naturally be selected. That the education of the youth is properly included within the functions of a municipal government cannot be denied * * *. As school houses are essential aids in the promotion of education, their erection is but inci-

§ 429. **The power to issue bonds under Nebraska statutes.**— The Supreme Court of Nebraska reversed the lower court and ordered an injunction to issue in this action of a taxpayer to restrain the issuing, registering and selling of certain school district bonds by the board of education. They held as to the power of the school district to issue these bonds that under the law as it stood prior to April 5, 1893, a district school board, except in cities of the metropolitan class, had no power to call an election on the question of issuing bonds for purchasing sites or erecting school houses until a petition had been presented to the board suggesting that such a vote be taken and signed by at least one-third of the qualified voters of the district. The presenting of such a petition was a condition precedent to a valid election. They further held that where the law requires a petition of a certain character in order to confer power upon a board to call an election for the purpose of issuing bonds or authorizing a tax, the determination of that board is not conclusive of the sufficiency of

dental to the maintenance of the schools, and falls as completely within the functions of a municipal government as does the erection of a hospital for its indigent poor or buildings for its fire engines; and the school houses, when so erected, are as fully municipal buildings as are its engine houses and hospital buildings. Danielly *v.* Cabannis, 52 Ga. 222; Horton *v.* Mobile School Comrs., 43 Ala. 598. See, also, Board of Education *v.* Fowler, 19 Cal. 24; Board of Education *v.* Martin, 92 Cal. 209. * * * The provisions of sections 1880–1887 of the Political Code for the issuance by the supervisors of the county of school district bonds, whenever the electors of the district shall vote therefor, to pay for the building of school houses in the district, do not limit or qualify the power conferred by [the statute first mentioned] upon an incorporated city to issue its own bonds for the same purpose, notwithstanding the provisions of section 1576 of the same code, making such incorporated city a school district. Each of these acts is a general law upon a subject within legislative power, and if there is any inconsistency between them that which is later in date must prevail over the earlier act. * * * A school district has not, like an incorporated city, any financial officers, nor has it been intrusted with the power of assessment and taxation which is conferred upon an incorporated city, and for these reasons, as well as others, the legislature would naturally intrust to the supervisors of the county, as being the body having the financial supervision of the school district, the function of issuing and providing for the payment of school district bonds; and as by the Constitution bonds cannot in any case be issued except upon a vote of two-thirds of the qualified electors of the district voting upon the question of their issuance, the agency by which they might be executed would seem immaterial, and there would be little likelihood of an issuance being authorized to be made for the same purpose by each agency."

the petition or the qualifications of the petitioners. These subjects are open to inquiry in judicial proceedings to nullify the action where the parties complaining have not by acquiescence or laches estopped themselves from contesting the question.[1]

§ 430. When bonds are void under Nebraska statutes.—Certain school district bonds of a district in Nebraska were involved in this action. The statutes under which they were issued were in these words: The act of February 15, 1869, provided that "Any school district shall have power and authority to borrow money to pay for the sites of school houses, and to erect buildings thereon, and to furnish the same, by a vote of a majority of the qualified voters of said district present at any annual meeting or special meeting; provided, that a special meeting for such purpose shall be upon a notice given by the director of such district at least twenty days prior to the day of such meeting, and that the whole debt of any such district at any time, for money thus borrowed, shall not exceed five thousand dollars." The act of February 27, 1873, to provide for the registration of certain municipal bonds, provides that "* * it shall be the duty of the president or township and school district boards or officers, * * * to register with the county clerk all precinct or township and school district bonds voted and issued pursuant to * * * [certain sections of the act to establish a system of public instruction for the state]." And the section prescribes the duty of the county clerk as to the registry of such bonds. On each of the bonds sued on there was a recital that it was issued "in pursuance of an act of the legislature of the state of Nebraska, entitled 'An act to establish a system of public instruction for the state of Nebraska,' approved February 15, 1869, and acts amendatory and supplemental thereto." In the lower court there was a judgment for the school district. The United States Circuit Court of Appeals for the eighth circuit affirmed the judgment, holding that these acts did not confer

[1] Fullerton *v.* School District of Lincoln, (Neb. 1894) 59 N. W. Rep. 896. In support of the first point the court cited and quoted from State ex rel. Phillips *v.* School Dist. No. 9, 10 Neb. 544; s. c., 7 N. W. Rep. 315; Kimball *v.* School Dist. No. 4, 13 Neb. 82; s. c., 12 N. W. Rep. 812; Orchard *v.* School Dist., 14 Neb. 378; s. c., 15 N. W. Rep. 730; State *v.* Babcock, 21 Neb. 187; s. c., 31 N. W. Rep. 682; Wullenwaber *v.* Dunigan, 30 Neb. 877; s. c., 47 N. W. Rep. 420.

authority to issue negotiable securities, and that the negotiable bonds issued by the school district here were void even in the hands of an innocent purchaser.[1]

§ 431. Validity of bonds as affected by constitutional restriction upon indebtedness of municipal corporations.—The Constitution of Iowa provides as follows: "No county, or

[1] Ashuelot Nat. Bank of Keene *v.* School Dist. No. 7, Valley County, (1893) 56 Fed. Rep. 197, affirming 41 Fed. Rep. 514. THAYER, D. J., speaking for the court in support of the ruling, said: "In the case of Merrill *v.* Monticello, 138 U. S. 673, 681; s. c., 11 Sup. Ct. Rep. 441, it was held that although a municipal corporation has an implied power to borrow money and to give written evidence of the indebtedness in the form of a note or bond, yet that it has no authority, as an incident of such power, to issue a negotiable security. It was further held that the power to borrow money and the power to give a negotiable bond which may circulate in the market freed from all equitable defenses, are essentially different powers, and that the latter power will not be implied from the former. In a later case (Brenham *v.* Bank, 144 U. S. 173; s. c., 12 Sup. Ct. Rep. 559) it was held that a city which had an express power under its charter 'to borrow for general purposes not exceeding fifteen thousand dollars on the credit of the city,' had no authority, as an incident of such power, to issue negotiable securities. In accordance with that view certain negotiable bonds, in the hands of an innocent purchaser, were declared to be void, although another provision of the charter of the city declared that 'bonds of the corporation of the city of Brenham shall not be subject to tax under this act,' and although the latter clause could only have had reference to bonds issued in pursuance of the power to borrow money for general purposes on the credit of the city. In speaking of the scope of the decision in Brenham *v.* Bank, Mr. Justice HARLAN, in the dissenting opinion, says: 'It seems to us that the court in the present case announces for the first time that an express power in a municipal corporation to borrow money for corporate or general purposes does not, under any circumstances, carry with it by implication, authority to execute a negotiable promissory note or bond for the money so borrowed. * * * A declaration by this court that such notes and bonds are void because of the absence of express legislative authority to execute negotiable instruments for the money borrowed will, we fear, produce incalculable mischief.' 144 U. S. 196, 197; s. c., 12 Sup. Ct. Rep. 568. It is unnecessary for us to assert that the decision last referred to goes to the full extent last indicated, of holding that a municipal corporation can only acquire authority to issue negotiable securities, by a statute which confers such power in express language, and that the power will not be implied under any circumstances. We think, however, that we may fairly affirm that the two authorities heretofore cited do establish the following propositions: *First*, that an express power conferred upon a municipal corporation to borrow money for corporate purposes does not in itself carry with it an authority to issue negotiable securities; *second*, that the latter power will never be implied, in favor of a municipal corporation, unless such

other political or municipal corporation, shall be allowed to become indebted in any manner, or for any purpose, to an amount in the aggregate exceeding five per centum on the value of the taxable property within such county or corporation, to be ascertained by the last state and county tax lists previous to the incurring of such indebtedness." A school district in that state, already indebted in a sum exceeding the limit named here at the time of the date of their issue, issued certain bonds in themselves aggregating a sum nearly $500 in excess of the limit. The bonds were issued at the same time and in one transaction. The whole issue were purchased in one purchase by the holder, who brought an action in the federal court upon them against the district. The United States Supreme Court held that the bonds were invalid by reason of the violation of the constitutional provision in their issue; and, further, it was held that the holder could not claim to be a *bona fide* purchaser no matter what recitals appeared on the face of the bonds.[1] The directors of a school district, the indebted-

implication is necessary to prevent some express corporate power from becoming utterly nugatory; and, *third*, that in every case where a doubt arises as to the right of a municipal corporation to execute negotiable securities the doubt should be resolved against the existence of any such right. The application of these principles to the case at bar satisfies us that the judgment of the Circuit Court was for the right party and should not be disturbed."

[1] Nesbit *v.* Riverside Independent District, (1892) 144 U. S. 610. Mr. Justice BREWER, speaking for the majority of the court, said: "If not charged with knowledge of the prior indebtedness, [the holder of the bonds] was with the fact that, independent of such indebtedness, these bonds alone were an overissue and beyond the power of the district; for she was bound to take notice of the value of taxable property within the district as shown by the tax list. Buchanan *v.* Litchfield, 102 U. S. 278; Northern Bank *v.* Porter Township, 110 U. S. 608; Dixon County *v.* Field, 111 U. S. 83. In the first of these cases, on page 289, it is said that 'the purchaser of the bonds was certainly bound to take notice, not only of the constitutional limitation upon municipal indebtedness, but of such facts as the authorized official assessments disclosed concerning the valuation of taxable property within the city for the year 1873;' and in the last, on page 95, that 'the amount of the bonds was known. It is stated in the recital itself. It was eighty-seven thousand dollars. The holder of each bond was apprised of that fact. The amount of the assessed value of the taxable property is not stated, but, *ex vi termini*, it was ascertainable in one way only, and that was by reference to the assessment itself, a public record equally accessible to all intending purchasers of bonds, as well as to the county officers.' So when the plaintiff purchased these bonds she knew, or at least was chargeable with knowledge of the fact, that they were unlawfully issued and created no obligation against the district."

ness of which already exceeded that allowed by the constitutional limitation, having contracted an indebtedness with certain parties, and afterwards, through collusion, permitted them to obtain judgment for the same against the school district upon proceedings to compel the authorities of the school district to levy taxes for the payment of this judgment, it was held by the Supreme Court of Iowa that the judgment was of no validity against the district and could not be enforced.[1] In an action upon certain bonds issued by a school district of Iowa in the federal court, which were held to be invalid, as in violation of the constitutional provision of that state limiting the indebtedness to be incurred by such a corporation, it was pressed upon the United States Supreme Court that a judgment obtained by the holder of these bonds, the plaintiff here, in the state court upon two coupons detached from these bonds operated as an estoppel of the district to contest the validity of the bonds in the federal court. The court held that the defense was open to the district.[2]

[1] Kane & Co. *v.* Independent School District of Rock Rapids, (1891) 82 Iowa, 5. See as to incurring indebtedness in excess of the limitation upon municipalities, the duty of creditors, the right to attack such indebtedness on the part of the municipality, etc., French *v.* City of Burlington, 42 Iowa, 614; Independent District *v.* Schreiner, 46 Iowa, 172; Kelley *v.* Town of Milan, 127 U. S. 139; s. c., 8 Sup. Ct. Rep. 1101.

[2] Nesbit *v.* Riverside Independent District, (1892) 144 U. S. 610. *Arguendo,* it was said by the court: "The law in respect to such estoppel was fully considered and determined by this court in the case of Cromwell *v.* County of Sac, 94 U. S. 351. It was there decided that when the second suit is upon the same cause of action, and between the same parties as the first, the judgment in the former is conclusive in the latter as to every question which was or might have been presented and determined in the first action; but when the second suit is upon a different cause of action, though between the same parties, the judgment in the former action operates as an estoppel only as to the point or question actually litigated and determined, and not as to other matters which might have been litigated and determined. * * * Each matured bond is a separable promise, and gives rise to a separate cause of action. It may be detached from the bond and sold by itself. Indeed, the title to several matured coupons of the same bond may be in as many different persons, and upon each a distinct and separate action be maintained. So, while the promises of the bond and of the coupons in the first instance are upon the same paper, and the coupons are for the interest due upon the bond, yet the promise to pay the coupon is as distinct from that to pay the bond as though the two promises were placed in different instruments upon different paper. By the rule laid down in Cromwell *v.* Sac County the judgment in the suit [in Iowa] is conclusive in this case only as to the matters litigated and determined. What

§ 432. Bonds secured by a pledge of school fund and property.— The bonds of a city of Kansas issued by the board of education of the city, secured by a pledge of the school fund and property of the city with coupons attached, have been held

were they ? The defense pleaded was this: That at the time the bonds were issued the indebtedness exceeded five per cent, and the bonds were, therefore, void; that the district received no consideration, and that the plaintiff was not a *bona fide* holder. The judgment entry shows that it appeared from the evidence that the indebtedness at the time the bonds were issued exceeded the constitutional limitation of five per cent, but that it was adjudged that the recitals in the bonds estopped the defendant from showing this fact against the plaintiff. In other words, that which was determined was the effect of the recitals. But this case does not turn upon that question at all, and nothing was determined here antagonistic to the adjudication there. An additional fact, that of notice from the amount of the bonds purchased, was proved. The effect of recitals in municipal bonds is like that given to words of negotiabilty in a promissory note. They simply relieve the paper in the hands of a *bona fide* holder from the burden of defenses other than the lack of power, growing out of the original issue of the paper, and available as against the immediate payee. * * * In the suit [in Iowa] no notice to the holder was shown. The recitals cut off the defense pleaded of original invalidity. In this action notice is proved, and an additional fact is put into the case which makes a new question. The effect of recitals is one thing; that of recitals coupled with notice is another. The one question was litigated and determined in [the Iowa] suit; the other is presented here. Surely an adjudication as to the effect of one fact alone does not preclude in the second suit an inquiry and determination as to the effect of that fact in conjunction with others. * * * It was well said in Cromwell *v.* County of Sac, page 356, that 'Various considerations other than the actual merits may govern a party in bringing forward grounds of recovery or defense in one action which may not exist in another action upon a different demand, such as the smallness of the amount, or the value of the property in controversy, the difficulty of obtaining the necessary evidence, the expense of the litigation and his own situation at the time. A party acting upon considerations like these ought not to be precluded from contesting in a subsequent action other demands arising out of the same transaction.' This case may be looked at in another light. The defense pleaded in [the Iowa] suit was, that at the time of the issue of the two bonds then disclosed, there was a prior indebtedness of the district exceeding the constitutional limitation; and that defense was the one adjudged to be precluded by the recitals. Here are additional defenses, that the five bonds in suit themselves created an overissue. That question was not presented in [the Iowa] suit, and could not have been adjudicated. It is presented for the first time in this case. It is of itself a valid defense, irrespective of prior indebtedness. So we have in this case a new question not presented in [the Iowa] suit, the existence of facts never called to the attention of the court in that case, which of themselves create a perfect defense."

by the United States Supreme Court to be valid obligations of the municipal corporation.[1]

§ 433. **Conditions precedent to the issue of bonds.**— In a case from Kansas involving the validity of certain bonds issued by the board of education of the city, which required the consent

[1] Atchison Board of Education *v.* De Kay, (1893) 148 U. S. 591. Mr. Justice BREWER, speaking for the court, after reviewing the Kansas legislation as to cities, stated the objections to the validity of the bonds and replied to them as follows: "*First*, it is objected that the bond purports to be issued under authority of an act entitled, 'An act to organize cities,' etc., approved February 28, 1868; that no such act is to be found in the statutes of that year, and that, therefore, the bonds were issued without authority of law, and are not valid obligations. This is trifling. There was an act giving authority to the board of education to borrow money and issue bonds, and whose title was exactly as described in this bond, except in place of the word 'organize' the word 'incorporate' was used. *Falsa demonstratio non nocet.* Commissioners *v.* January, 94 U. S. 202. An error in copying into an instrument a single word in the title of a statute does not vitiate the deliberate acts of the proper officers of a municipality as expressed in the promise to pay, which they have issued for money borrowed. Again, it is insisted that the board of education had no power to bind the city of Atchison as a municipal corporation, but only that other and *quasi* corporation known as school district No. 1, Atchison county. The argument is that there were two corporations: *First*, a school district corporation whose name and corporate existence were prescribed by the Laws of 1858; and another, a strictly municipal corporation, known as the city of Atchison, with the ordinary powers attached to such a municipality; that though they embraced within their limits the same territory and population, they were in fact distinct corporate entities, and that the board of education, having control of the affairs of the corporation, had no power to bind the other by its promise to pay." The court said: "It may well be doubted whether there were two distinct corporations. Section 14 of the acts of 1867 and 1868, incorporating cities of the second class, provided that 'each city shall constitute at least one school district.' There is no pretense, under the power reserved in that section, that the city of Atchison was ever divided into districts; so, by that section, Atchison city constituted a school district. The members of the board of education were to be elected at the annual city election, and to the board was given full control of the school affairs of the city. Section 57. In other words, it was the city's schools and the city's school property, which were placed under the management of the board of education. Upon the report of the board of education the city council levied and collected the school taxes (section 67), and when they were collected they were retained by the city treasurer in his custody. Section 68. The title to all school property was vested in the city. Section 70. No bonds could be issued without the consent of the city council. Section 76. And the school fund and property of such city is pledged to the payment of the bonds. Section 81. The whole idea of the

of the city council, the record showed a number of meetings of a part of the council, and adjournments to subsequent dates, one of these adjournments when only the clerk of the council was present. At a final meeting the mayor and five councilmen, being a majority of the council, were present, and a resolution was passed giving the consent of the council to the issue of these bonds. It was insisted before the United States Supreme Court that consent could only be given by an ordinance, and not by resolution.[1] Further, it was contended that even if a resolution were sufficient, there was no legal meeting of the council, because all the members were not present, and it did not appear that all were notified, or that a special meeting had been called; that it was not a regular, but apparently an adjourned meeting; and that the first adjournment was without validity because none of the councilmen were present, and the adjournment was ordered by the clerk alone.[2] The Supreme Court held these bonds to be valid.[3]

statute seems to have been the mingling of the schools and the school interest with the ordinary municipal functions of the city of Atchison, giving to the board of education, as an administrative body of the city, the management of the schools and the school property. Further, when in 1872 a new act was passed in respect to the incorporation of cities of the second class, * * * it was expressly provided that 'the public schools of such city organized in pursuance of this act, shall be a body corporate, and shall possess the usual powers of a corporation for public purposes by the name and style of 'The Board of Education of the city of ——, of the state of Kansas,' and in that name may sue,' etc. The legislation seems to imply that up to that time there was in cities of the second class no separate school corporation. But even if this be a misconstruction of the statute, it is clear that the school district and the city were coterminous; that, by the act of 1868, the board of education was authorized to borrow on the credit of the school property, with the consent of the city council, and to issue bonds in payment therefor. They did proceed, as appears from the recital in the bonds, under authority given by that act, and if there were a misrecital of the name of the obligor, such mere misrecital would not vitiate the obligations. Proceeding strictly under that act, they bound the corporation whose officers they were and for which they assumed to act, and whether the name of that corporation was technically 'The City of Atchison' or 'School District No. 1, Atchison County,' by the issue of bonds they bound that corporation."

[1] In support of this position the case of Newman *v.* Emporia, 32 Kans. 456, was cited.

[2] In support of these last positions the cases of Paola & Fall River Railroad *v.* Anderson County Comrs., 16 Kans. 302, and Aikman *v.* School District, 27 Kans. 129, were cited.

[3] Atchison Board of Education *v.* De Kay, (1893) 148 U. S. 598. Mr.

§ 434. The adoption of a statute to obtain authority to issue bonds — mode of calling election.—The adoption, by a vote of the electors of a city, at an election duly called in accordance with the provisions of the city charter, of an act relating to schools pursuant to the provisions of that act, the United States

Justice BREWER, speaking for the court, said: "In respect to the first of these contentions the general rule is that where the charter commits the decision of a matter to the council, and is silent as to the mode, the decision may be evidenced by a resolution, and need not necessarily be an ordinance. State *v.* Jersey City, 27 N. J. L. 493; Butler *v.* Passaic, 44 N. J. L. 171; Barb Wire Co. *v.* Chicago, Burlington, etc., Railway, 70 Iowa, 105; Sower *v.* Philadelphia, 35 Pa. St. 231; Gas Company *v.* San Francisco, 6 Cal. 190; First Municipality *v.* Cutting, 4 La. Ann. 335; Green Bay *v.* Brauns, 50 Wis. 204; 1 Dill. Mun. Corp. (4th ed.) § 307 and notes. Nor is there anything in [Newman *v.* Emporia, 32 Kans. 456] in conflict with this. That simply holds that where a charter requires that certain things be done by ordinance they cannot be done by resolution. In this act incorporating cities of the second class there is nothing which either in terms or by implication requires that the consent of the city council shall be given only by ordinance. A resolution was, therefore, sufficient." As to the contentions as to the meetings of the council and the adjournment by the clerk of one of them, it was said: "The act of 1868, section 13, provides that regular meetings of the city council shall be held at such times as the council may provide by ordinance. No evidence was offered showing what were the dates of regular meetings, as provided by ordinance. We are led to infer that these meetings were not regular meetings from the language at the commencement of the records thereof — 'that council met pursuant to adjournment.' The first adjournment was made by the city clerk alone, no member of the city council being present. We are not advised by the testimony as to what rules, if any, had been prescribed by the city council in respect to such matter. It is not an uncommon thing for legislative bodies, such as a city council, to provide by rules that, in the absence of all members, the clerk or secretary shall have power to adjourn. That probably such a rule as that was in existence is evidenced by the fact that at succeeding meetings, which, giving full weight to the language used at the commencement of the record, were simply adjourned meetings, the council, all but one of whom were present at one of the meetings, approved the records. All these entries of meetings appear to have been kept upon the regular record of the city council, and it is obvious that either because an adjournment by the clerk in the absence of the council was authorized by rule, or because the days of the subsequent meetings were, in fact, the regular days therefor, such meetings were accepted and recognized by the council as legal. Certain it is that when bonds have been issued in reliance upon a consent thus evidenced, and when for years thereafter interest has been duly paid upon such bonds, the court will not, after the lapse of twenty years, in a suit on the bonds, pronounce them invalid on such technical and trivial grounds." The court then distinguished the cases relied on on behalf of the city (Paola & Fall River Railroad *v.* Anderson

Circuit Court of Appeals for the eighth circuit held was not void because a resolution of the city council calling the election, which was not required by any provision of the statute or the charter, never took effect because it was not legally published. The bonds sued upon in this action were issued under the act referred to above relating to schools, and it was contended that it was never legally adopted by the city, and the bonds were, therefore, void.[1]

County Comrs., 16 Kans. 302, and Aikman *v.* School District, 27 Kans. 129) to show that they did not militate against the views of the court, before given, as follows: "In the case in 16 Kansas, which was an action by the county against the railway company to cancel a subscription for stock, and for the return and cancellation of bonds of the county on deposit with the state treasurer, the matter was submitted on demurrer to the petition and that petition averred that the subscription was ordered at a special session of the board, at which only two of the three commissioners were present; that no call for such session was made, nor anything done to authorize a call; that B. M. Lingo, the absent commissioner, was in the county, at his residence, but had no knowledge or notice of such intended special session; 'that knowledge and notice of such intended special session was intentionally and fraudulently concealed and kept from said B. M. Lingo by the said railway company and its agents; and said session was not a regular session of said board, nor was it an adjourned session from any regular session thereof, nor from any duly called special session of said board.' The court held that the subscription ordered under those circumstances was not binding upon the county. In that case the contract was executory, and the bonds had not been delivered, but were still within the control of the county. The special session, with only a fraction of the board present, was fraudulently intended and fraudulently brought about, and the railway company was the wrongdoer. The illegality of the session was not a matter of inference, but a fact alleged and admitted. The case in 27 Kansas is even stronger. That was a suit on a written contract, signed by two members of a school district board, the board consisting of three. Such a contract could only be made by the district board as a board. It appeared affirmatively that there was no meeting of the board; that it was signed by the two members, not after consultation, but by each separately, and at a different time from the other."

[1] National Life Ins. Co. of Montpelier *v.* Board of Education of City of Huron, (1894) 62 Fed. Rep. 778. The court distinguished National Bank of Commerce *v.* Town of Granada, 54 Fed. Rep. 100; s. c., 4 C. C. A. 212, cited in support of the contention, in these words: "In that case the bonds were issued under [a statute] of Colorado which expressly provides that the city council or board of trustees shall call the election and shall publish the notice of the election to determine whether or not the bonds shall issue, and shall then issue the bonds if the vote is favorable. The board of trustees of the town of Granada passed an ordinance which in itself called the election, presented the notice and authorized the mayor and clerk to issue the bonds if the vote was favorable. A general statute of the state provided that such an ordinance should be published and that it should not take effect

§ 435. When non-compliance with the requirements of the Constitution of the state is not a defense against bona fide purchasers.— In a late case before the United States Circuit Court of Appeals for the eighth circuit, the board of education, authorized to issue bonds, issued them without complying with a constitutional requirement of South Dakota that, at or before the time of incurring such indebtedness, provision should be made for the collection of an annual tax to pay interest and principal, although the board had full power to make such provision. The bonds recited "that all conditions and things required to be done precedent to and in the issuing of said bonds have duly happened and been performed in regular and due form as required by law." The court held that the non-compliance with such requirement was not available to the board as a defense against *bona fide* purchasers of the bonds. This board were authorized to issue bonds for certain purposes and to sell them for not less than ninety-eight cents on the dollar. They issued bonds purporting to be for such purposes, but, in fact, for an unauthorized purpose, accepted a bid from an individual for the bonds at par, and delivered them to him, received part of the price, and

until five days after its publication. The ordinance never was published, and the court held that it was never in force, and that the mayor and clerk never had any authority to issue the bonds; that it was a case of total want of authority on their part to act upon any conditions. McClure *v.* Township of Oxford, 94 U. S. 429, is a similar case of want of authority, because in that case the statute had not taken effect before the notice of election was given, so that there was no authority to give it. But these cases have no relevancy to the question presented here. In the case of the Town of Granada the statute required the board of trustees to call the election and to publish the notice of it. There is no such provision relative to the election for the adoption of article 3 in any of the statutes under which the bonds were issued. That article provides that any organized city may at any time adopt the provisions of the act by a majority vote of the electors. It is silent as to the person or body that shall call the election and as to the notice of it." The facts are then stated as to the election called here, and it is said: "At that election the electors voted, the city council subsequently canvassed and declared the vote, and all parties treated it as a valid election until they came to pay these coupons. In that election every requirement of the charter and of the statute was complied with, and in our opinion the election was valid and article 3 was duly adopted. If the city council had passed no resolution calling the election, it would yet have been called and held in strict accordance with the charter, and that election cannot be invalidated by the fact that the city council passed a futile resolution that never took effect."

transferred its right to the balance to the city, receiving a city warrant for the amount. This individual, whose bid was accepted by the board, sold the bonds for ninety-seven and a half cents on the dollar. The court held that this constituted an executed sale of the bonds to this individual at par, and purchasers from him, who were strangers to his purchase from the board, were not chargeable with notice of the invalidity of the bonds, because they supposed they were buying from the board. And, as against innocent purchasers for value, before maturity, of bonds issued by a city board of education, it was no defense that the board loaned nearly the entire proceeds of their sale to the city for city warrants that were never paid, and that could not be legally enforced.[1]

§ 436. **When the defense that the site of the school house was not owned by the district is not open in a bona fide holder's action on the bonds.**— One of the most recent cases involving the question of what defenses are open in actions upon municipal bonds by *bona fide* purchasers and owners was one involving the liability of a school district in North Dakota upon bonds issued under a special act of the legislature authorizing the issuance of bonds. The Supreme Court of that state held that there was no error in rejecting the offer on the part of the defendant to prove that the land on which the school building for which the bonds in suit were issued was situated was not owned by the defendant or its school board, which was a condition prescribed in the statute to the issuing of bonds; that it had never been conveyed to the district or its school board; that proceedings to condemn it as a school site had never been instituted; and that it was in fact the property of a third person. There was an express provision in an amendment to the special act that the indebtedness of no school district mentioned in the original act should be bonded until the land on which the school

[1] National Life Ins. Co. of Montpelier *v.* Board of Education of the City of Huron, (1894) 62 Fed. Rep. 778. SANBORN, Circuit Judge, further said: "That a municipal corporation has given away or squandered the proceeds of negotiable securities which it placed upon the market, cannot affect the rights of *bona fide* purchasers who had no knowledge of, nor part in, the gift or waste. They are in no way responsible for the wise and economical use by the corporation of the funds it borrows. County Comrs. *v.* Beal, 113 U. S. 227, 240; s. c., 5 Sup. Ct. Rep. 433; Cairo *v.* Zane, 149 U. S. 122, 137; s. c., 13 Sup. Ct. Rep. 803; Maxcy *v.* Williamson Co., 72 Ill. 207."

building was located should have been conveyed by good and sufficient warranty deed to the school board of such district, or the title to it should have been obtained by the school board by proper condemnation in the manner prescribed by law. The Supreme Court said of this: "The existence of this fact of ownership of the site on which the school building was situated was a condition precedent to the existence of any power to issue bonds. Until this fact existed, the district was as powerless to bond as if no statute on the subject had been passed." Then it was said: "The only possible escape of the plaintiff from this conclusion is by invoking another doctrine — the doctrine of estoppel from recitals in the bonds or in a certificate attached to it." Upon each bond was indorsed a certificate signed by the county clerk, certifying that such bond "is issued in accordance with law and by authority of a majority of the legal voters of said district present and voting at an election duly held May 11, 1885, for that purpose, and is duly registered in this office." The court held that the school district was estopped by this recital to make the defense suggested.[1]

§ 437. **When the defense that the proceeds of bonds were used for another purpose is not open in such an action.**— It was held in this case that it was not a defense to the bonds, as against *bona fide* purchasers of them, that the citizens and officers of the municipal corporation, with intention to use the proceeds of the bonds for an unlawful purpose, took the necessary steps to issue them for a lawful purpose, certified on the face of them that they were issued for such lawful purpose, and then appropriated the proceeds to an unlawful purpose.[2]

Flagg *v.* School District No. 70, (N. D. 1894) 58 N. W. Rep. 499. The doctrine of estoppel is very fully discussed in the opinion rendered by the court.

[2] National Life Ins. Co. of Montpelier *v.* Board of Directors of City of Huron, (1894) 62 Fed. Rep. 778. The court said: "Corporations are as strongly bound to an adherence to truth in their dealings with mankind as are individuals, and they cannot, by their representations or silence, induce others to part with their money or property and then repudiate the obligations for which the money was expended, and which their statements represented to be valid. The defendant, in its resolutions and records, in all the resolutions and records of the city council of Huron, in the call for and vote at the election which authorized the issue of the bonds, and in the bonds themselves, declared that they were issued for a lawful purpose, viz., 'To raise funds for the purchase of a school site and for the erection of a school building thereon.' The present

§ 438. What does not create an estoppel of the district to defend.— In case the officers of a school district, without lawful authority, borrow and expend money for the completion of a school house, the Supreme Court of Minnesota has held that no liability attaches to the district therefor, notwithstanding the benefit received from the expenditure, and that no estoppel or ratification can be inferred from the retention or enjoyment of the improvement by the school district, as it had no option to reject the improvement.[1] In an action upon certain school district bonds received in exchange for bonds, which were void under the provisions of the Constitution of Iowa limiting the amount of indebtedness of counties and municipal corporations to five per cent of the value of taxable property therein, it appeared that the bonds were issued to the owner of the old bonds, not a *bona fide* holder, under an act of the legislature of that state empowering school districts to issue refunding bonds. The federal court held that no estoppel arose, from recitals in the refunding bonds, to prevent a showing that the constitutional limitation was

holders purchased them and paid for them with no notice or knowledge that they were issued for any other purpose, and in the full belief that these declarations were true. It is no defense, as against these *bona fide* purchasers, that this corporation, during all this time, intended to use, and has since used, the money it raised from these bonds for the unlawful purpose of conducting a campaign for the state capitol. It is no defense that it knew at the time it was taking these proceedings and making these declarations that they were false, and that during all this time it intended, *first*, to deprive itself of the school site and building; and, *second*, to deprive the purchasers of the bonds of the moneys they paid for them on the faith of its representations, and that it has accomplished the former purpose, and now seeks, with the aid of the courts, to accomplish the latter. Such a plea cannot be entertained in a court of justice. The corporation is estopped to deny that these bonds were issued to raise money for a school site and school buildings. Moran *v.* Commissioners, 2 Black, 722; Hackett *v.* Ottawa, 99 U. S. 86, 90; Ottawa *v.* National Bank, 105 U. S. 342, 345; Zabriskie *v.* Railroad Co., 23 How. 381; Omaha Bridge Cases, 10 U. S. App. 101, 189; s. c., 2 C. C. A. 174; 51 Fed. Rep. 309; Paxson *v.* Brown, 61 Fed. Rep. 874, and cases cited."

[1] Young *v.* Board of Education of Independent School District No. 47, (Minn.) 55 N. W. Rep. 1112. It was said by the court: "It would be a very unsafe rule to establish to hold that school officers might borrow money at their pleasure, and bond the district because the same is expended by them in improving the property of the district. The case is to be distinguished from Borough of Henderson *v.* County of Sibley, 28 Minn. 515; s. c., 11 N. W. Rep. 91. There the money claimed had been deposited in the county treasury, and was used and expended by the county in the erection of a court house, which it had authority to

exceeded in the prior issue. Further, the purchaser of such refunding bonds was bound to take notice of the listed value of the property of the school district.[1]

§ 439. **One of the latest decisions on the effect of recitals in bonds.**—In a very late case as to the effect of recitals upon the face of bonds issued by municipal corporations upon the rights of *bona fide* holders of such bonds, the United States Circuit Court of Appeals for the eighth circuit, as their conclusion after a review of many of the leading cases upon this subject, declared these rules: Where a municipal body has lawful authority to issue bonds or negotiate securities, dependent only upon the adoption of certain preliminary proceedings, and the adoption of those preliminary proceedings is certified on the face of the bonds by the body to which the law intrusts the power and upon which it imposes the duty to ascertain, determine and certify this fact before or at the time of the issuing of the bonds, such a certificate will estop the municipality, as against a *bona fide* purchaser of the bonds, from proving its falsity in order to defeat them. Such an estoppel may arise in a proper case, upon a recital that an act required by a Constitution has been performed, as well as upon a recital of the performance of an act required by statute. Recitals in municipal bonds may constitute an estoppel in favor of a *bona fide* purchaser, even where the body that issued the bonds had no power to issue them, and could not, by any act of its own or of its constituent body, make a lawful issue of the bonds, if the fact of this want of power does not appear from the bonds the purchaser buys, the Constitution and statutes under which they are issued nor the public records referred to therein. But recitals in municipal bonds by the representative body that issues them, to the effect that all the requirements of the laws with reference to their issue have been complied with, will not estop the municipality from proving, as against a *bona fide* purchaser, that the representative body had no power to issue them where no act of the representative or constituent body could make

build. It was expended for a lawful purpose by the proper authorities, and the county could not deny that it had, or had used for its benefit, plaintiff's money received without consideration, and was bound to refund."

[1] Shaw *v.* Independent School Dist. of Riverside, (1894) 62 Fed. Rep. 911, following Doon Township *v.* Cummins, 142 U. S. 366; s. c., 12 Sup. Ct. Rep. 220, reversing Cummins *v.* District of Doon, 42 Fed. Rep. 644.

the issue lawful at the time it was made, and this fact appears from the Constitution and statute under which the bonds are issued, the public records referred to therein and the bonds the purchaser buys.[1]

[1] National Life Ins. Co. of Montpelier *v.* Board of Education of City of Huron, (1894) 62 Fed. Rep. 778. The cases reviewed and cited by the court from which they drew their deductions were: Dixon Co. *v.* Field, 111 U. S. 83; s. c., 4 Sup. Ct. Rep. 315; Sutliff *v.* Commissioners, 147 U. S. 230; s. c., 13 Sup. Ct. Rep. 318; Northern Bank of Toledo *v.* Porter Tp. Trustees, 110 U. S. 608; s. c., 4 Sup. Ct. Rep. 254; McClure *v.* Township of Oxford, 94 U. S. 429; Lake Co. *v.* Graham, 130 U. S. 674; s. c., 9 Sup. Ct. Rep. 654; Nesbit *v.* Independent District, 144 U. S. 610; s. c., 12 Sup. Ct. Rep. 746; Hedges *v.* Dixon Co., 150 U. S. 182; s. c., 14 Sup. Ct. Rep. 71; Marsh *v.* Fulton Co., 10 Wall. 676; Buchanan *v.* Litchfield, 102 U. S. 278; Pana *v.* Bowler, 107 U. S. 529; s. c., 2 Sup. Ct. Rep. 704; Oregon *v.* Jennings, 119 U. S. 74; s. c., 7 Sup. Ct. Rep. 124; Chaffee Co. *v.* Potter, 142 U. S. 355; s. c., 12 Sup. Ct. Rep. 216; Commissioners *v.* Aspinwall, 21 How. 539; Bissell *v.* City of Jeffersonville, 24 How. 287; Moran *v.* Commissioners, 2 Black, 722; Meyer *v.* City of Muscatine, 1 Wall. 384, 393; Lee Co. *v.* Rogers, 7 Wall. 181; Pendleton Co. *v.* Amy, 13 Wall. 297, 305; City of Lexington *v.* Butler, 14 Wall. 282; Grand Chute *v.* Winegar, 15 Wall. 355; Lynde *v.* Winnebago Co., 16 Wall. 6; Marcy *v.* Township of Oswego, 92 U. S. 637; Town of Coloma *v.* Eaves, 92 U. S. 482; County of Moultrie *v.* Rockingham Ten Cent Sav. Bank, 92 U. S. 631; Commissioners *v.* Bolles, 94 U. S. 104; Commissioners *v.* Clark, 94 U. S. 278; Commissioners *v.* January, 94 U. S. 202; County of Warren *v.* Marcy, 97 U. S. 96.

CHAPTER XXII.

MUNICIPAL AID BONDS — COUNTY.

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§ 440. **County aid bonds, generally.**— The governing boards of counties, where the authority has not been conferred upon them to issue bonds in payment of a subscription to stock of a railroad company by an election properly called, will not be compelled to issue such bonds.[1] Under authority for the issue of bonds of municipal corporations and apply their proceeds as subscription to railroad stock, the railroad company to be aided thereby may take the bonds themselves at par in exchange for stock.[2] When

[1] Schuyler County *v.* People, 25 Ill. 181; Clarke *v.* Supervisors of Hancock County, 27 Ill. 305; Fulton County *v.* Mississippi & Wabash Railroad, 21 Ill. 373; People *v.* Tazewell County, 22 Ill. 147. The Court of Appeals of Virginia upheld the power of a county to subscribe for stock to a railroad company under the provisions of the charter of the company and its amended charter, and affirmed a judgment dismissing the bill praying to enjoin the issue and sale of bonds for the purpose of paying the subscription in Powell *v.* Supervisors of Brunswick County, (1892) 88 Va. 707. See, also, Taylor *v.* Board of Supervisors, 86 Va. 506.

[2] Decker *v.* Hughes, 68 Ill. 33. Subscriptions to stock of railroad or other corporations entitled thereto under au-

the steps have been taken required by a statute authorizing an issue of bonds by a county in payment of a subscription to the stock of a railroad company, the provisions of the statute being fully complied with, and the denomination of the bonds not specified in the statute, a county may issue one bond or more, as the authorities may find convenient or deem proper. Should the authorities afterwards take up one bond which they may have issued covering the whole amount, and in exchange for it issue a greater number in smaller denominations covering the subscription, and the county, by its action, subsequently recognize the issuance of the bonds in smaller denominations given in exchange, this will be deemed a satisfaction of the bonds.[1] The stipulation between a railroad company and a county issuing its bonds to the company, upon delivering them to the bankers of the company, that the bonds were to be applied in payment for work done within the county and not elsewhere, has been construed to mean, in view of this purpose, not that these identical bonds should pay for work done in that county, but that if work was done in the county the bonds should be delivered to the company.[2] Should a county receive stock in a railroad company to the full amount of its subscription, and vote its stock and pay interest on the bonds issued in payment of its subscription, the county cannot be heard to say that it was not liable to pay accruing interest on the bonds.[3] The Supreme Court of Tennessee has held that the fact

thority of the legislature by municipal corporations must conform to the mode prescribed in the law. W. & Mt. S. P. R. Co. *v.* Clarke County Ct., 3 Metc. (Ky.) 143; Mercer Co. Ct. *v.* Ky. River Navigation Co., 8 Bush (Ky.), 307.

[1] Johnson *v.* County of Stark, (1860) 24 Ill. 75.

[2] Thomas *v.* Morgan County, 59 Ill. 479.

[3] Board of Supervisors of Mercer County *v.* Hubbard, (1867) 45 Ill. 139. As to what will not operate to estop a county from denying that an election in favor of aid to a railroad company was properly held, or to relieve the company claiming the benefit of the subscription from the burden of showing that the election was properly held, see People *v.* Jackson County, 92 Ill. 441. An act of Kansas authorizing the issue of bonds held unconstitutional and the bonds held void. C. B. U. P. R. R. Co. *v.* Smith, 23 Kans. 745. When a corporation is qualified to accept the benefits of the Kansas statute enabling municipal townships to subscribe to stock, etc., of railroad companies. Atchison, Topeka & Santa Fe R. R. Co. *v.* Jefferson County, 21 Kans. 309. When an action can be maintained by a county to have bonds surrendered for cancellation as not being legal and binding upon the county. Anderson County *v.* Paola & Fall River Ry. Co., 20 Kans. 534; P. & F. R. Ry. Co. *v.* Anderson County, 16 Kans. 302. Donation of land by a county to a railroad company in aid of its construction held absolutely void, though author-

that the act of the legislature authorized the bonds to be issued in aid of a railroad company, bearing interest at the legal rate where they were payable, in another state where the rate of interest allowed was larger than in Tennessee, did not render the bonds void for usury.[1] A railroad company receiving bonds of a county on a subscription to its preferred stock, and agreeing to pay the interest on the same until the road should be completed into the county, will not be bound for the interest after the county has received and become entitled to interest on its preferred stock, though the stock may have been received before the completion of the road into the county.[2] And the county having received the stock, in an action to recover such interest from the company, will be estopped to set up that the road had not been completed, or that the act of the county authorities in receiving the stock was *ultra vires*.[3]

ized by the legislature, in Ellis *v.* Northern Pac. R. R. Co., 77 Wis. 114; s. c., 45 N. W. Rep. 811. As to the constitutionality of the act of the legislature of Kansas authorizing aid to railroad companies by subscription to stock of, and issue of bonds to, such companies, see Morris *v.* Morris County, 7 Kans. 576. That the preliminary steps to a subscription and issue of bonds prescribed by the act authorizing it must be strictly taken, see Lewis *v.* Bourbon Co., 12 Kans. 186.

[1] Nelson *v.* Haywood County, 3 Pickle, 781; s. c., 11 S. W. Rep. 885.

[2] County of Lancaster *v.* Cheraw & C. R. R. Co., 28 S. C. 134; s. c., 5 S. E. Rep. 338.

[3] Ibid. As to the authority of municipal corporations to make donations in aid of railroads, see Madry *v.* Cox, 73 Tex. 538; s. c., 11 S. W. Rep. 541; MacKenzie *v.* Wooley, 39 La. Ann. 944. As to the right of taxation and the duty of the authorities for the payment of subscriptions to stock of railroads by municipal corporations, see Meriwether *v.* Muhlenburg Co. Ct., 120 U. S. 354; s. c., 7 Sup. Ct. Rep. 563; Bartemeyer *v.* Rohlfs, 71 Iowa, 582; s. c., 32 N. W. Rep. 673; Chicago, M. & St. Paul Ry. Co. *v.* Hartshorn, 30 Fed. Rep. 541. Where it was held that an agreement by the railroad company to which aid was voted under the Kansas statutes, executed after the subscription of the county, to sell and transfer its road after it was completed, in order to obtain money for its construction, did not discharge or release the county from the payment of its subscription, see Southern Kansas & P. R. R. Co. *v.* Towner, 41 Kans. 72; s. c., 21 Pac. Rep. 221. That taxpayers may be estopped to deny the validity of a tax voted in aid of a railway corporation by a municipal corporation by an expenditure on the part of the railroad corporation of large sums in the construction of its road, and the taxpayers making no objection, see Johnson *v.* Kessler, 76 Iowa, 411; s. c., 41 N. W. Rep. 57. Aid bonds were issued by a county in West Virginia, and placed in the hands of three citizens of the county as a committee, to be delivered in such amounts as in their judgment would be a fair compensation for work done in the county upon the road, on which work these bonds were to be expended. The Supreme

Where an unconditional subscription has been made by a county to stock of a railroad company, under legal authority, the contract will be complete, and creditors of the company may rely upon it for payment of their debts as implicitly as upon any other assets of the company, although the company may subsequently abandon all proceedings under its charter on account of its insolvency.[1] And the president of the railroad company, while he might bind himself, and the creditors and stockholders of the company might bind themselves, by an agreement to treat a subscription of this sort as conditional, so far as their respective rights are concerned, the president has no right or authority to make such an agreement so as to prejudice the company or its creditors.[2] The Supreme Court of Alabama, one justice, however, dissenting, has held that under the Constitution of that state, the legislature has power to authorize a county, as a body corporate, to subscribe for stock in a railroad company, if the people chose to do so, by a popular vote to that effect. Also, they held that for the payment for the stock so subscribed, the county, as a corporation, might be authorized and required to issue bonds of the county and deliver them to the railroad company, to the stock of which the county might subscribe, in the manner prescribed by law.[3] All reasonable presumptions will be indulged in favor of the regularity of county bonds issued and put into circulation upon subscription to the stock of a railroad company, until overcome and rebutted. Even if irregularities are shown, the bonds will

Court held that the contract of the county was not impaired by the County Courts' adopting an ordinance requiring the bonds still undelivered to be countersigned by the president of the County Courts, who should concur in and approve their delivery, the committee being mere agents of the county. Satterlee *v.* Strider, 31 W. Va. 781; s. c., 8 S. E. Rep. 552.

[1] Morgan County *v.* Thomas, 76 Ill. 120.

[2] Ibid.

[3] Ex parte Selma & Gulf Railroad Co., (1871) 45 Ala. 696. That a legislature has the constitutional right to authorize counties and cities to become shareholders in railroad companies, see Johnson *v.* County of Stark, (1860) 24 Ill. 75; followed in Perkins *v.* Lewis, (1860) 24 Ill. 208. That the building of a railroad is a corporate purpose for which subscription may be made to the stock of and bonds issued to a railroad corporation, see Nichol *v.* Mayor & Aldermen of Nashville, 9 Humph. (Tenn.) 252; Louisville & Nashville R. R. Co. *v.* County Court, etc., 1 Sneed (Tenn.), 637; Goddin *v.* Crump, 8 Leigh (Va.), 120; Talbot *v.* Dent, 9 B. Mon. (Ky.) 526; Thomas *v.* Leland, 24 Wend. 65; Slack *v.* Maysville & Lexington R. R. Co., 13 B. Mon. (Ky.) 1; Commonwealth *v.* McWilliams, 1 Jones (Pa.), 61; People *v.* Mayor of Brooklyn, 4 Comst. 419; Shaw *v.* Dennis, 5 Gilm. (Ill.) 405.

not be invalidated thereby unless they go to the power of the authorities of the county to issue them.[1] In an Alabama case the Supreme Court held that mere irregularities, not fraudulent, which may have intervened in the exercise of the authority to make the subscription and issue the bonds for its payment, must be held to be waived, if not objected to prior to the issuance of the bonds and the performance by the railroad corporation of its part of the duty imposed, in consideration of the aid thus afforded.[2] A bond purporting upon its face to be issued under

[1] Maxcy *v.* Williamson County, 72 Ill. 207.

[2] Fielder *v.* Montgomery & Eufaua R. R. Co., (1874) 51 Ala. 178, affirming a dismissal of the bill praying an injunction in this case. *Arguendo*, the court said: "It seems now to be the settled law that where the power to make the subscription and to issue the bonds, or to impose a tax necessary for its payment, is once shown to exist, the obligation to pay cannot be denied or repudiated. The consent to the 'subscription,' is a consent to the issuance of the bonds, and an obligation to pay them, and it is a consent also to the tax necessary for this purpose, if that is the mode allowed by law for raising the funds required for their payment. Ex parte Selma & Gulf R. R. Co., 45 Ala. 696, 730, 731. Here the corporations were fully organized on both sides, and capable of contracting to the full extent of the obligations each undertook to perform; and they substantially pursued the mode authorized by law for this purpose. Speaking upon this important question the Supreme Court of the United States, quoting the language of the Supreme Court of Wisconsin, says: 'The power of municipal corporations when authorized by the legislature to engage in works of internal improvement, such as the building of railroads, canals, harbors, and the like, or to loan their credit in aid thereof, and to defray the expenses of such improvements, and make good their pledges by an exercise of the power of taxing the persons and property of their citizens, *has always been sustained*, on the ground that such works, although they are in general operated and controlled by private corporations, are, nevertheless, by reason of the facilities which they afford for trade, commerce, and intercommunication between different and distant portions of the country, indispensable to the public interests and public functions. It was originally supposed that they would add, and subsequent experience demonstrated that they have added, vastly and almost immeasurably, to the general business, commercial prosperity, and pecuniary resources of the inhabitants of cities, towns, villages, and rural districts through which they pass and with which they are connected. It is in view of these results, the public good thus produced, or other benefits thus conferred upon the persons and property of all the inhabitants composing the community, that courts have been able to pronounce them matters of public concern, for the accomplishment of which the taxing power might lawfully be called into action.' Olcott *v.* The Supervisors, 16 Wall. 678, 691, 692; Hasbrouck *v.* Milwaukee, 13 Wis. 37. In this important case, the highest judicial tribunal in the nation declares, in effect, that if the power to make the subscription, and to issue the bonds for its payment, *exists at the time of*

authority of a special act of the legislature, will, as a rule, be invalid if that act is unconstitutional, and should it be sought to uphold the bond by virtue of authority given in some other act of the legislature, to sustain the bond even in the hands of a *bona fide* purchaser, it must appear that the terms of the act relied upon have in fact been complied with, and that the bond is in fact legal and valid, as issued in aid of some public and authorized purpose.[1] Bonds of a county in Kansas had been properly issued under authority in aid of a railroad company, and afterwards, under authority of legislative act, the county took up these bonds and issued funding bonds in exchange for them, changes beneficial to the county being made in their terms. A portion of the county had in the meantime been detached from the county. The Supreme Court held that though the funding bonds were technically both authorized and issued after the detachment of this portion of its territory, yet, within the spirit of the law, and legally, the funding bonds were a charge against the detached territory the same as the railroad aid bonds for which they were exchanged had been.[2] The Supreme Court of Illinois refused a *mandamus* to compel a county to issue $20,000 in bonds of the county to a railroad company for $20,000 in its shares of stock to be immediately returned to the company upon payment of two dollars on its part, according to the terms upon which this subscription of the county was entered upon the subscription books of the company, upon the ground that such an agreement to sell and transfer that amount of stock for two dollars was fraud *per se* and the court could not recognize or enforce it as valid or obligatory.[3] A county subscribing to the stock of, and issuing bonds in payment to, a railroad corporation, existing at the time as a matter of fact, the question whether the corporation had then a legal existence cannot be raised in an action on the bonds, this being a question between the railroad and the state.[4] It is no defense against a third person who is an

the subscription and issuance of the bonds, their obligation must be complied with, and this obligation will be enforced by the national power."

[1] C. B. U. P. R. R. Co. *v.* Smith, 23 Kans. 745.

[2] Marion County *v.* Harvey County, 26 Kans. 181.

[3] County Court of Macoupin County *v.* People ex rel., etc., (1871) 58 Ill. 191.

[4] Dallas County *v.* Huidekoper, (1880) 14 Sup. Ct. Rep. 1190, following Smith *v.* County of Clark, 54 Mo. 59. The same question is considered in County of Macon *v.* Shores, 97 U. S. 272, 276.

innocent purchaser for value that there was fraud in the issue of bonds given by a county in aid of a railroad.[1] Even when allowable such defense must be set up before judgment; it cannot be interposed to an action to enforce the judgment.[2] The fact that a railroad company, which has received the bonds of a county issued to it under a law authorizing the same, but requiring that the railroad company shall not sell them for less than par, does sell such bonds below par will not affect the right of the holder of the bonds to recover principal and interest at par.[3]

§ 441. **Elections to authorize aid bonds — how called — how questions must be submitted to voters — how result determined, etc.**— The particular county authorities upon whom is conferred the power to call an election upon the question of subscriptions to the stock of a railroad company, must call the election. If called by any other authority their action will be simply void for want of power.[4] Where an election on the question of a subscription by a county to the stock of a railroad company, and issuance of bonds in payment of the subscription, is called by the wrong public authority, the bonds issued under such an election, though issued by the proper public authority, would be absolutely void. The fact that a majority of the votes at such an election may have been in favor of the subscription would not relieve the election and subsequent issue of the bonds from their illegality.[5] Where the power of counties to contract with a railway corporation to subscribe to its capital stock is dependent upon its being authorized by a vote of the people, the county authorities cannot hold out any offer to the railway corporation prior to a vote upon which the corporation has a right to rely.[6] As a rule, where there is fraud and illegality in the elec-

[1] Muscatine *v.* Mississippi & M. R. R. Co., 1 Dill. 536.

[2] Ibid.

[3] Richardson *v.* Lawrence County, (1864) 14 Sup. Ct. Rep. 1157. See, also, Woods *v.* Lawrence County, 1 Black, 386.

[4] Gaddis *v.* Richland County, 92 Ill. 119; Jacksonville, N. W. & S. E. R. R. Co. *v.* Virden, 104 Ill. 339. As to steps preliminary to an election, see People *v.* Town of Oldtown, 88 Ill. 202; Fulton County *v.* Mississippi & Wabash R. R. Co., 21 Ill. 338; Lippincott *v.* Town of Pana, 92 Ill. 24.

[5] Supervisors of Marshall County *v* Cook, (1865) 38 Ill. 44. In which case the board of supervisors were the proper authorities to order the election under the law as it then stood, and the election was ordered by the County Court, and the bonds were issued by the board of supervisors.

[6] People *v.* Cass County, 77 Ill. 438.

tion, the officers of the municipal corporation have no power to validate such election by acts and admissions.[1] In an Indiana case the county attempted to evade its liability upon the bonds issued by the county authorities upon the ground that informalities had occurred in giving the notice and in conducting the election to determine whether the county would, or not, authorize a subscription to the stock of the railroad company, contending that these irregularities rendered the bonds and coupons void. The Supreme Court held the county liable upon the bonds and coupons.[2] Where the act authorizing a subscription of this kind requires the name of the railroad company to be specified as the recipient of the aid, a vote to aid in the construction of a railroad along a certain route would give no authority to the commissioners of a county to subscribe to stock of, or issue bonds to, any corporation.[3] The modus of procuring a subscription by a county to the stock of a railroad corporation, payable in the bonds of the county, under the provisions of the Alabama statute authorizing such subscriptions, was as follows: "The said railroad companies, by their *president and a majority of their directors*, may, in writing, propose to any such county that it shall subscribe for and take an amount of their capital stock, to be named in said proposal, at a certain price per share, and pay for the same in the

[1] People *v.* Logan County, 63 Ill. 374; People *v.* Cline, 63 Ill. 394.

[2] Johnson *v.* County of Stark, (1860) 24 Ill. 75. The court said: "In the case of Prettyman *v.* Tazewell County, 19 Ill. 406, it was held that if such irregularities had occurred it was necessary, for the purpose of preventing the officers from proceeding to make the subscription and to issue the bonds, that steps must be promptly taken by an appropriate remedy to contest the election and restrain them from proceeding; and that we must not inquire after any considerable delay whether fraudulent means had been resorted to for the purpose of procuring a favorable result to the election of subscription. It would be manifestly against every principle of justice to permit the taxpayers and citizens of a county, through their officers, to procure money, labor or materials upon bonds of the county, issued on an affirmative vote of the citizens at an election held in a case authorized by the law to escape all liability because of some slight informality in conducting the election which was, or at least might have been, readily known to any citizen of the county before the bonds were issued. Counties have no right to procure all the benefits of an act which they are authorized to perform, recognized and voted upon by them as legal, and then escape liability any more than have private individuals. They must respond to their legal engagements to the same extent as individuals."

[3] Gulf Railroad Co. *v.* Miami County, 12 Kans. 230; Lewis *v.* Bourbon County, 12 Kans. 186.

bonds of the county, as shall be set forth in said proposal." "That upon the application of the *president and directors of any of the railroad companies of Alabama*, to the Commissioners' Court of any county of the same, submitting proposals for a county subscription to the capital stock of said railroad company, the Commissioners' Court of said county in which application is made, is hereby authorized and required to order an election within sixty days after the meeting of said court, to submit the proposition of said railroad company to the qualified electors of said county, for their acceptance or rejection." In a case where a proposal was made for a subscription by the corporators of a railroad company, in which the signers were styled, one as president and the others as directors, but there had been no election of officers by the stockholders of the corporation, as required by the law governing such corporations, and the county commissioners had ordered an election and declared the vote in favor of the subscription by the county, and were about to issue county bonds to the railroad corporation in conformity with the vote, the Supreme Court held that such proposal by the corporators was not such as the statute contemplated and provided, and that the election ordered and held was void, and that there was no power in the county commissioners either to make the subscription or to issue the bonds of the county in payment of such subscription, and reversed the decree of the chancellor dismissing the bill praying an injunction and remanding the same for further proceedings.[1] They also held that the proceedings for the subscription, vote and bonds in this case were not in substantial compliance with the act authorizing subscriptions by counties, and, therefore, the later statute, proposing to legalize subscriptions, etc., of this kind on the part of counties, had no curative effect in this case.[2] It is not necessary, under the General Railroad Law of Missouri, that the

[1] Trammell *v.* Pennington, (1871) 45 Ala. 673.

[2] Ibid. Rules as to a majority of voters under statutes authorizing aid to railroad corporations. McDowell *v.* Rutherford Ry. Construction Co., 96 N. C. 514; s. c., 2 S. E. Rep. 351; Kentucky Union Ry. Co. *v.* County of Bourbon, 85 Ky. 98; s. c., 2 S. W. Rep. 687; Wood *v.* Commissioners of Oxford, 97 N. C. 227; s. c., 2 S. E. Rep. 653. Illustrations of notices of elections for a vote of aid to railroads held to satisfy the requirements of the statutes. Yarish *v.* Cedar Rapids, I. F. & N. W. Ry. Co., 72 Iowa, 556; s. c., 34 N. W. Rep. 417, following Burges *v.* Mabin, 27 N. W. Rep. 464; Bartemeyer *v.* Rohlfs, 71 Iowa, 582; s. c., 32 N. W. Rep. 673. An election for an issue of bonds in place of other aid bonds that had matured, held not necessary under the constitu-

order submitting to the voters of the county a proposition to subscribe to stock in a railroad company should specify the name of the corporation, where the proposition describes the proposed route of the road with the requisite certainty.[1] An election upon the question of granting aid to railroad corporations may be contested, and its validity determined in a proceeding directly for that purpose, notwithstanding the facts that the county commissioners may have subscribed for shares of the capital stock of the railroad corporations, and the latter may have made contracts based upon such subscription.[2] Where a charter for a railroad company provided that the County Court of a county in Ken-

tional provisions of North Carolina in Blanton *v.* Board of County Commissioners, 101 N. C. 532; s. c., 8 S. E. Rep. 163.

[1] Ninth National Bank *v.* Knox County, 37 Fed. Rep. 75. See, also, Kentucky Union Ry. Co. *v.* County of Bourbon, 85 Ky. 98; MacKenzie *v.* Wooley, 39 La. Ann. 944; Young *v.* Railroad Co., 75 Iowa, 140; State *v.* Harris, 96 Mo. 29; Onstott *v.* People, 123 Ill. 439. In Nelson *v.* Haywood County, 3 Pickle, 781; s. c., 11 S. W. Rep. 885, an election ordered by the County Court on the question of "bonds" or "no bonds," and the return of the officer holding the election showed that this was the proposition actually voted on, was held to be in accordance with the statute of Tennessee, though it might be inferred from the officer's return that the election was on bonds to be given in subscription for the stock. Where, under a statute of Iowa, notice by publication in a newspaper of an election for a tax in aid of a railroad corporation was held not to be required. Johnson *v.* Kessler, 76 Iowa, 411; s. c., 41 N. W. Rep. 57. In Christian County Court *v.* Smith, (Ky.) 12 S. W. Rep. 134, an election at which the question of subscribing to the capital stock of two different railroad companies was submitted, was held to be null and void under the statute of Kentucky prohibiting more than one question of taxation to be submitted to the voters at one election.

[2] Goforth *v.* Rutherford Ry. Construction Co., 96 N. C. 535; s. c., 2 S. E. Rep. 361. That taxpayers of a county may maintain an action in the proper court to declare a subscription on the part of a county to stock of a railroad corporation void, and to enjoin the collection of a tax to pay it on the ground of the illegality of the election authorizing the subscription, see Kentucky Union Ry. Co. *v.* County of Bourbon, 85 Ky. 98; s. c., 2 S. W. Rep. 687. In State ex rel. *v.* Nemaha County, 10 Kans. 569, where there had been an election authorizing a subscription to the stock of a railroad company, but before the subscription had been actually made under authority granted in the general law in force at the time of the election the company had consolidated with another, the authority to make the subscription was held to have been terminated and that the county was not bound by an attempted subscription to the stock of the consolidated company by the commissioners, their action being *ultra vires.* Bonds of a county in Tennessee containing a recital that they were issued under the act authorizing them, having been delivered to a railroad company and interest paid on them for fifteen years, the Supreme

tucky might submit the question whether the court should subscribe to the capital stock of the railroad company on behalf of the county, either absolutely or upon conditions, the Court of Appeals held that the County Court was the judge of the character of the proposition it would present, and had discretionary power to submit or not the question to the voters of the county, who had the ultimate power of adoption or rejection.[1] But if, after the County Court had prepared the conditions of the contemplated subscription, and submitted them to the people, and the vote taken had resulted in favor of the adoption of the conditions, the County Court could not revoke its action and order a second vote, as it would be assuming legislative functions for it so to do.[2] And where the terms of the order of the County Court submitting the proposition provided that if the vote was favorable the county judge should, upon proof that the conditions precedent had been complied with, order the clerk to make the subscription, the action of the county judge would be conclusive, if he had not acted fraudulently or in bad faith.[3] A county in Kentucky was authorized by statute to subscribe to the stock of a railroad company upon condition that the holders of real estate in the county should, by a majority, vote for such subscription, and the question was submitted by the County Court to all the voters of the county. The Court of Appeals held this submission to have been not such as the statute required, and a levy of tax to pay such subscription to be invalid.[4] The statute in this case also provided "that before subscription should be made and the tax levied, the question of levying the tax should be submitted to the voters of the county, and if a majority of the votes cast should be in favor of the tax it should be levied." The Court of Appeals held that the submission of the question of making a subscription to the stock of railroad company alone, without submitting the question of levying the tax, did not authorize the levying of the tax.[5] The Supreme Court of Alabama held that

Court of that state held that the county could not set up an irregularity in the election as against an innocent purchaser of the bonds. Nelson *v.* Haywood County, 3 Pickle, 781; s. c., 11 S. W. Rep. 885.

[1] Madison County Court *v.* Richmond, Irvine & T. F. R. R. Co., 80 Ky. 16.

[2] Ibid.

[3] Ibid.

[4] Bullock *v.* Curry, 2 Metc. (Ky.) 174.

[5] Ibid. Validating subscriptions by legislative action. Shelby County Ct. *v.* C. & O. R. R. Co., 8 Bush (Ky.), 218. Power of the legislature after a vote is taken. C. & O. R. R. Co. *v.*

a writ of *mandamus* should be granted to enforce the subscription of a county to stock in a railroad company, and the issuance of the bonds of the county in payment of the subscription to the stock, which had been voted in pursuance of the act of Alabama, authorizing such subscriptions, by the people of counties, where the Court of County Commissioners refused to comply with the requirements of the act, upon the ground that the act was void for want of conformity to the Constitution of the state.[1] The charter of an Illinois railroad company authorized certain counties through which the road was to pass to subscribe to stock therein, making it the duty of the board of supervisors of the several counties, upon the application in writing of the board of directors of the road, to order an election in the counties upon the question of making the subscription, etc. It also provided "that, should the voters of such county refuse to vote such subscription, the board of directors, by a petition signed by at least two hundred legal voters of such county, presented to the board of supervisors thereof, may require them to submit the same proposition to the voters of such county at any subsequent general or county election." The board of directors acted under the provisions of the charter, and applied to the county authorities for a subscription to a certain amount; an election was held and the county refused to vote the subscription. The board of directors then presented a petition with the requisite number of voters, as required by the last provision, requesting a submission of the same question at the next election. The Supreme Court held that the board of supervisors were not warranted in refusing the petition on the ground that the president of the railway company having alone acted in the matter, therefore, the petition had not been regularly presented, it appearing that his action was authorized by a resolution of the board of directors. And, it having also been objected by the supervisors that no evidence existed of the fact of the genuineness of the petition, and the board of directors of the company, therefore, having offered to make the necessary proof thereof, which was refused, the court held that,

Barren County Ct., 10 Bush (Ky.), 610.

[1] Ex parte Selma & Gulf R. R. Co., (1871) 45 Ala. 696. As to the power of the legislature in such cases, see Stein *v.* Mayor of Mobile, 24 Ala. 591; Stein *v.* Mayor of Mobile, 17 Ala. 234. See, also, Von Hoffman *v.* City of Quincy, 4 Wall. 535; Mitchell *v.* Burlington, 4 Wall. 270, 274; Thompson *v.* Lee County, 3 Wall. 330; Meyer *v.* City of Muscatine, 1 Wall. 385; Gelpcke *v.* City of Dubuque, 1 Wall. 202.

while the board of supervisors of the county might have acted upon it as genuine, without proof, or might have required proof that the petitioners were legal voters of the county; yet, by their refusal to hear such proof they would be regarded as having waived it. The court also construed the provisions of the charter upon this subject, and held that, when the request was made as directed, the board of supervisors were bound to submit the proposition to a vote of the county; that they had no discretion in the matter nor as to the amount so asked to be subscribed, the power to fix the amount having been conferred upon the directors of the company; that the board of supervisors had the power only in case the subscription was voted to withhold it so long as any two of the counties named in the act should fail or refuse to vote for such subscription, as also the power to fix the interest upon the bonds issued, and the time of their payment within the limits fixed by the act.[1] Should a county pay interest on bonds issued by it in payment of subscription to the stock of a railroad company, and vote on the stock it may have received for the bonds, and the bonds have passed into the hands of innocent purchasers without notice, the county will not be allowed to urge any mere irregularities in the election on the question of issuing the bonds, so as to defeat a recovery upon the bonds or the coupons thereto attached.[2] An act authorizing the subscription to stock of, and issue of bonds to, a railroad company, provided for bonds "drawing interest at the rate of ten per cent per annum." The question submitted to the voters at the election was as to subscribing for stock and issuing bonds therefor, to bear not to exceed ten per cent interest. The action of the voters in voting in favor of this proposition was construed as an assent to the issue of bonds bearing the rate prescribed by the act.[3] It would be a good defense on the part of a county to an application for *mandamus* to compel the issuing of bonds to a railroad company that the majority of the votes at the election held to authorize it was made up of illegal votes; that a majority of the legal votes cast at the election was against the subscription, and that the company had notice, before entering into liabilities, of the character of the vote.[4]

[1] People ex rel. Prettyman *v.* Board of Supervisors of Logan County, (1867) 45 Ill. 162.

[2] Board of Supervisors of Mercer County *v.* Hubbard, (1867) 45 Ill. 139.

[3] People *v.* Board of Supervisors of Ford County, (1872) 63 Ill. 142.

[4] People *v.* Board of Supervisors of Logan County, 63 Ill. 374. When elections authorizing aid bonds by a

This was an action in the federal court by a holder of overdue interest coupons, upon municipal bonds issued by a county in Mississippi in payment of a subscription by the county to the capital stock of a railroad company. The Constitution of that state provides that: "The legislature shall not authorize any county, city or town to become a stockholder in, or to lend its credit to, any company, association or corporation, unless two-thirds of the qualified voters of such county, city or town, at a special election or regular election to be held therein, shall assent thereto." It was claimed before the Supreme Court of the United States, on behalf of the county, that the qualified voters referred to in the Constitution and the charter of the railroad company were those who had been determined by the registrars to have the requisite qualifications of electors, and who have been enrolled by them as such, and that it required a vote of two-thirds of the whole number enrolled as qualified voters, and not merely two-thirds of such actually voting at an election for that purpose. The question presented, therefore, by this claim to the Supreme Court, under the plea of the county, that "the board of supervisors fraudulently and illegally issued and delivered the bonds and coupons," had reference, as viewed by the court, merely to the bonds being issued without the alleged requisite assent of two-thirds of the registered vote. It was held that the assent of two-thirds of the qualified voters at an election lawfully held for that purpose, to a proposed issue of municipal bonds, intended by the Constitution of the state, meant two-thirds of the qualified voters present and voting at such election in its favor, as determined by the official return of the result; that the words "qualified voters," as used in the Constitution, must be taken to mean not those qualified and entitled to vote, but those qualified and actually voting.[1] It has been held in the federal court that, under the provision of the Constitution of Mississippi, which declares that the legisla-

county under Kentucky statutes were held to have been void. Christian County Court *v.* Smith, (Ky.) 13 S. W. Rep. 276. An election for such bonds under Kansas laws held void because of want of a sufficient petition. Chicago, K. & W. R. R. Co. *v.* Comrs., 43 Kans. 760; s. c., 23 Pac. Rep. 1064. The submission of a proposition to the voters which was held not to invalidate the bonds in the hands of innocent purchasers. Williams *v.* People, (Ill.) 24 N. E. Rep. 647.

[1] Carroll County *v.* Smith, (1884) 111 U. S. 556, following St. Joseph Township *v.* Rogers, 16 Wall. 644, and County of Cass *v.* Johnston, 95 U. S. 360, and declining to accept the rule declared in Hawkins *v.* Carroll County, 50 Miss. 735.

ture shall not authorize any county, city or town to aid any corporation, unless two-thirds of the qualified voters of such municipality shall assent thereto at a special election, railroad aid bonds were not invalidated in the hands of innocent purchasers by the fact that less than such majority voted for them, where more than two-thirds of the votes cast were in favor of issuing the bonds.[1] The *gravamen* of a bill filed by the supervisors of a county in Mississippi to enjoin the further payment of certain bonds issued by the county in aid of a railroad company, is thus stated in the opinion of the Supreme Court of that state, rendered by WOODS, Ch. J.: "The *gravamen* of complainant's bill is that these bonds are invalid, because the subscription to the capital stock of said railroad company and the issuing of the bonds were not made after two-thirds of the qualified voters had signified their assent thereto, as required by the Constitution of the state and the act of the legislature passed in that behalf. The bill does not deny that the respondents are *bona fide* holders of the bonds and without notice of the alleged irregularity complained of as rendering the bonds invalid; but the ground relied upon is, that the respondents, though purchasers without notice in the usual acceptation of that term, are yet not to be protected, for the reason that their innocence in this case is only and really their ignorance of the essential facts, as is alleged, that less than two-thirds of the qualified voters of the county assented to the subscription to the capital stock of said railroad company, and that this essential fact was and is a matter of public record equally accessible to all persons, being contained in the registration lists of the voters of the county. In other words, this is the underlying proposition on which the contention of the bill of complaint rests, namely, that though an election was conducted under the forms and in accordance with the provisions of the act of the legislature; though the board of supervisors examined the returns made to it by the officers who managed the election, and, as the result of such examination, determined that two-thirds of the qualified voters had cast their ballots in favor of such subscription, nevertheless the bonds are invalid even in the hands of *bona fide* holders, for the reason that the board of supervisors had no authority or power to ascertain, determine and declare

[1] Madison County *v.* Priestly, Treasurer, (1890) 42 Fed. Rep. 817, following Carroll Co. *v.* Smith, 111 U. S. 556; s. c., 4 Sup. Ct. Rep. 539.

the essential fact that the requisite two-thirds of the qualified voters had assented to the subscription, this essential fact being referable to and determinable alone by a fixed standard, to wit, the registration lists of the voters of the county." The court held that whether the required vote had been cast to authorize these bonds, was a question determinable by the board of commissioners of the county, and was conclusive; that the county was estopped in this action by *bona fide* holders of the bonds to claim that they were invalid because they had not been authorized by a proper vote at the election held with reference to their issue.[1]

[1] Board of Supervisors of Madison County *v.* Brown, (1890) 67 Miss. 684. The court summed up its conclusions as follows: "Beginning with Knox County *v.* Aspinwall, 21 How. 539, and running through a long line of cases, ending with Township of Bernards *v.* Morrison, 133 U. S. 523, in which Mr. Justice BREWER delivered the opinion of the court, the Supreme Court of the United States has uniformly held that the ascertainment and determination of the essential fact of the assents of the required number of voters requisite to authorize subscriptions for stock and the issue of bonds, belong to the tribunal to which was confided the control of the matter. In the last-named case Mr. Justice BREWER observes: 'While it is true that the act does not in terms say that these commissioners are to decide that all preliminary conditions have been complied with, yet such express direction and authority is seldom found in acts providing for the issuing of bonds. It is enough that full control in the matter is given to the officers named.' And this conducts us to the conclusion that there is no foundation upon which to plant the contention of [the county's] counsel, that the Supreme Court of the United States has either overruled or modified any former decision, made in that form, along the line of kindred adjudication. There can be no room for skepticism as to the true doctrine in this state. In Vicksburg *v.* Lombard, 51 Miss. 111, it was said that 'if the constituted authorities of the city put the bonds on the market, or deliver them to the railroad company for sale on the assertion that the proper vote was given, the city ought to be estopped from setting up against the *bona fide* holder the plea that the assertion is untrue.' In Cutler *v.* Madison County, 56 Miss. 115. Chief Justice SIMRALL, speaking for the court, said: 'The statute under which these bonds were executed made it the duty of the board of supervisors to canvass the votes, and declare the result of the election. Their decision is conclusive on the county, in a controversy between it and a *bona fide* purchaser of the bonds.' In Madison County *v.* Paxton, 57 Miss. 701, Chief Justice GEORGE, in speaking of a part of the series of bonds involved in the present litigation, said: 'It will be noticed that there is no attempt to shelter Paxton's purchase under the rights which a purchaser from the company may have had, in case his purchase was *bona fide.* The overwhelming force of the two cases last cited as authority in the case at bar, will be acknowledged by any one when it is remembered that the bonds whose validity was there assailed, and in the case before us, are parts of the same issue.'"

The bonds involved here were county bonds, issued by a county in Missouri, in payment of a subscription to the stock of a railroad, which was to run through that county. There were a number of questions considered and adjudicated by the United States Supreme Court, bearing upon the election ordered and held in the county to authorize such bonds. The order for the election directed that notice thereof "be given, through the [local newspaper] for five weeks, and by printed handbills publicly exposed throughout the county." It also named the second Monday in March as the day for the election. No evidence was offered on the trial of any printed handbills, or of the publication of the notice in the newspaper. It was insisted that, in the absence of evidence, there could be no presumption that notice was given either by handbills or in the newspaper. Another insistment was that between the date of the order, February sixth, and the date of the election, March twelfth, it was not possible to make the prescribed publication because, excluding the day of the order and including the day of the election, there would be only thirty-four days, or one day lacking the five full weeks. The statutes of Missouri at that time in force provided, in accordance with the general rule in respect to such matters, that "the time within which an act is to be done shall be computed by excluding the first day and including the last."[1] Mr. Justice Brewer, speaking for the court, said, upon the objections: "But the notice required for this election was not prescribed by statute. It was fixed by order of the County Court, and there being but thirty-four days between the day of the order and that named for the election, it must be presumed that what was intended was not a publication for five full weeks of seven days each, but a publication in each of the five weeks, which could easily be made in the thirty-four days. It cannot be supposed that the County Court directed a notice which it was impossible to give, or that it was putting the people to the annoyance and the county to the expense of an election which was necessarily void by reason of an inability to comply with the terms of the order. The order must be construed so as to make possible a valid election, and that is accomplished by construing it, and in a reasonable way, as requiring advertisement in five successive weekly issues of the paper named.[2] The

[1] Gen. Stat. Mo. 1866, p. 84, § 6.

[2] Knox County *v.* Ninth National Bank, (1893) 147 U. S. 91, 96, 97.

provisions of the Constitution of Missouri adopted in 1865, that "the general assembly shall not authorize any county, city or town to become a stockholder in, or to loan its credit to, any company, association or corporation, unless two-thirds of the qualified voters of such county, city or town, at a regular or special election to be held therein, shall assent thereto," was invoked in behalf of the county issuing these bonds in aid of the Missouri and Mississippi Railroad Company resisting a recovery. The Supreme Court held that the validity of the bonds was not affected by that provision of the Constitution.[1] As to the objection made to the use of the words "bonus" in the submission of a proposition to the voters of a county in Illinois whether or not

[1] Knox County *v.* Ninth National Bank (1893), 147 U. S. 91. The court said: "At the October term, 1867, of the Supreme Court of Missouri the case of State *v.* Macon County Court, 41 Mo. 453, was decided, in which it was held that the Constitution had no retroactive effect upon statutes passed before its adoption, and that, therefore, under the Missouri and Mississippi Railroad Company Act, passed February 20, 1865, a few months before the adoption of the Constitution, there was power in the county authorities to subscribe without the assent of the voters. It may well be believed, as asserted by counsel for defendant in error, that, until that decision was announced, the understanding that the prohibition in the Constitution superseded all unexecuted authority given by prior charters was so general that no County Court would have dared to subscribe stock and issue bonds without the assent of two-thirds of the qualified voters. The subscription was made, some of the bonds issued, as well as the vote held, before the decision in the Macon County case, and it is difficult to believe that the County Court did not issue these bonds in reliance upon the authority given them by the vote of the people, in pursuance of the general laws of the state, although referring on the face of the bonds to the Missouri and Mississippi Railroad Company Act, which specially authorized the company to receive, and the counties through which it ran to make, subscriptions. It is very likely that the County Court had in mind the special act creating the Missouri and Mississippi Railroad Company, as well as the general law, and the vote of the people under it, and that it meant to exercise all the authority conferred by both. It is enough for this case that the vote of the people authorizing the issue of bonds was given, and that the County Court acted in reliance thereon, for, by assent, through their vote, to such issue of bonds, the people, in the way prescribed by the statutes of the state, in effect consented that the levy beyond the meagre one provided for by the Missouri and Mississippi Railroad Company Act might be resorted to for the payment of these bonds." As to the validity of an election authorizing county aid bonds to be issued to a railroad company, though no particular corporation as the recipient of the aid be designated, and that it is sufficient simply to designate the route, see Knox County *v.* Ninth National Bank, (1893) 147 U. S. 91; Commissioners *v.* Thayer, 94 U. S. 631; Scipio *v.* Wright, 101 U. S. 665.

its swamp lands should be appropriated in aid of the construction of a certain railroad run through the county, the Supreme Court of the United States said, in this case: "The objection to the word 'bonus' in the proposition submitted to the voters of Wayne county is not valid. This submission, in connection with the general subject of a failure to comply with the requisites prescribed by the statute, has been already discussed. Upon its individual merits we are also of the opinion that the objection is not valid. It is a verbal criticism merely — an objection to the words and not to the substance of the submission. A proposition was submitted to the voters, of which the affirmative was in these words: 'For appropriating the swamp lands of Wayne as a bonus to any company, for building a railroad through said county.' It is said that the word 'bonus' condemns the submission; that this means a gratuity, a voluntary donation, a gift, and that a town or county cannot, although it have the direct authority of the legislature, give away its property. When this question is properly before us it will be disposed of. It does not, however, arise in this case. In the first place, if it be assumed that the word is correctly defined as a gift or gratuity, that meaning is controlled and limited by the connection in which it is here used, to wit, that in consideration of it the company receiving the lands will undertake to build a railway through the county. It is not simply a *bonus*, but a bonus to any company who shall undertake the great task of building a railroad through the county, a task which it is loudly complained has not yet been performed by any one."[1] The bonds, in a case before the United States Supreme Court, stated that they were issued under the statute of Nebraska relating to the subject, to aid the company in improving the water power of the river for the purpose of propelling public grist mills, "and other works of public improvement of a public nature" in the precinct. It was objected that the latter part of the statement was indefinite, and the other works to be aided or improved, or propelled, should have been decided or identified, so that it might be seen they were works of internal improvement, within the Nebraska statute, and also because the proposition voted on must, in order to be a lawful one, have stated what the specific "other works" were. To this the court said: "It is a sufficient answer to this question to say that the petition states, and

[1] Kenicott *v.* Supervisors, (1872) 16 Wall. 452, 470, 471.

the demurrer admits, that the only work of internal improvement of a public nature for which the bonds were issued to the company, was the improvement of the water power of the Elkorn river for the purpose of propelling public grist mills in the precinct; that the improving of such water power for that purpose rendered it available and useful for propelling other works of internal improvement of a public nature, which were, or thereafter might be, constructed and located on that river in that precinct; that the improvement of the water power of that river, to aid which the bonds were issued and negotiated, consisted in constructing a canal for water power purposes in the precinct; and that the bonds and their attached coupons were issued and negotiated under and by virtue of a majority vote of the qualified voters of the precinct, and in pursuance of the act. Thus, there is a distinct statement, as well as an admission, that no work of internal improvement was covered by the vote or the issue of the bonds, other than the one of improving such water power for the purpose of propelling public grist mills in the precinct. The statement in the bonds in regard to propelling other works of an internal improvement of a public nature in the precinct, is explained by the allegation in the petition that the improving of the water power for the purpose stated rendered it available to propel other works of internal improvement of a public nature, then existing or which might be constructed on the river within the bounds of the precinct. But this was an incidental result, and aside from the only work in aid of which, or as notified to, or known by, the plaintiff, at the time of the sale and delivery of the bonds to him."[1]

[1] Blair *v.* Cuming County, (1884) 111 U. S. 363, 368, 369. The following cases, referring to bonds issued in aid of "public improvements" under the Nebraska statutes and the power to issue them, were reviewed by the court: Osborne *v.* County of Adams, 106 U. S. 181; Traver *v.* Merrick County, 14 Neb. 327; Osborne *v.* Adams County, 109 U. S. 1; Union Pacific Railroad *v.* Commissioners, 4 Neb. 450; United States *v.* Dodge County, 110 U. S. 156; State *v.* Thorne, 9 Neb. 458; Dawson County *v.* McNamar, 10 Neb. 276; Nosser *v.* Seeley, 10 Neb. 460; Seeley *v.* Bridges, 13 Neb. 547; Township of Burlington *v.* Beasley, 94 U. S. 310. As to enterprises which are so far of a public nature that private property may be appropriated to carry them on, they cited: Boston & Roxbury Mill Corp. *v.* Newman, 12 Pick. 467; Commonwealth *v.* Essex Company, 13 Gray, 239; Lowell *v.* Boston, 111 Mass. 454; Seudder *v.* Trenton Delaware Falls Co., 1 Saxt. (N. J. Ch.) 694; Beekman *v.* Saratoga & Schenectady R. R. Co., 3 Paige, 45.

§ 442. **Conditions to subscriptions — the right to prescribe, etc.**— Though the law authorizing aid by a county, by way of subscription to stock of, and issue of bonds to, a railroad company may be silent as to conditions of subscription, the municipality voting aid may lawfully impose conditions upon which the subscription will be made, and, until a compliance with such conditions, the county cannot be compelled to issue and deliver the bonds by mandamus.[1] Where conditions have been imposed by the vote of the people upon such a subscription, the county authorities cannot delegate to others the determination of the question whether or not the conditions have been complied with. They must determine that fact themselves, as the authorized agents of the people.[2] Where the subscription and issue of bonds is subject to conditions before the bonds can be delivered, the county authorities would have no lawful power to issue the bonds in blank as to date, and place them in the hands of trustees, to be dated and delivered when the conditions may be performed.[3] A county having submitted the question of taking stock in a railroad company subject to conditions, the conditions may be removed by a second submission of the entire question to the electors.[4] Where a vote of a county in favor of bonds in aid of a railroad company in Illinois had been coupled with conditions that the road should be located at a designated place, and that the subscription should not be paid until the road was constructed, it was held that this did not amount to a contract to subscribe when the conditions were performed; also, that if the county authorities had a discretion to subscribe on a vote without conditions, the annexing of conditions would not deprive them of its exercise.[5] A county having voted aid to a railroad company in building its road by a certain route, without any other conditions, it appearing that the company, by its charter, was not bound to locate its road on that route, but had a large discretion as to the route to be selected, the Illinois Supreme Court held that the board of supervisors had the right to impose conditions as to the permanent location of the road upon the route contemplated, and

[1] People *v.* Glann, 70 Ill. 232; People *v.* Holden, 91 Ill. 446.

[2] Jackson County *v.* Brush, 77 Ill. 59.

[3] Ibid

[4] Board of Supervisors of Mercer County *v.* Hubbard, (1867) 45 Ill. 139.

[5] People *v.* Cass County, 77 Ill. 438. The right to subscribe upon conditions. Land Grant Ry. & Trust Co. *v.* Davis County, 6 Kans. 256.

to make any delivery of the county bonds to depend upon the same, and that the company, by accepting such conditions, was bound by them in respect to its rights under the vote and subscription.[1] It was provided in the statute authorizing an issue of bonds by a municipality in aid of a railroad company that the proceeds be expended in the county, and the specific proposition submitted to the vote of the people was based upon this condition, and the railroad company agreed to expend the money raised in the county. It was held in a federal court that this agreement contemplated the negotiation of the bonds in the regular and ordinary way, and the keeping of the proceeds of the bonds separate from the other assets of the company, and that the proceeds should be expended in the county; that it followed from this that such bonds were not covered by a mortgage of the railway company in favor of which they were issued, covering all its real and personal property then owned or thereafter to be acquired by the company.[2] Though the authority of a board of county commissioners to issue bonds in aid of a railway company upon compliance with certain conditions carries with it no authority to waive the conditions, where there is a failure of the railway company to comply with one of the conditions in some minor respect, and notwithstanding the failure the commissioners acting in good faith issue the bonds, and the failure is a matter which is of public knowledge, a failure by the county to make any objections or take any proceedings, and payment of the interest on the bonds for a series of years, will work a ratification of the action of the commissioners, and the county will thereby be prevented from recovering of the railroad company the bonds or their value.[3] The statute of Kentucky providing that, before county bonds issued in the aid of a railroad are delivered, the president of railroad company shall give bond for the faithful application of

[1] Alley *v.* Adams County, 76 Ill. 101. What was not a compliance with a condition as to the location of a road, and the bonds invalidated thereby, though in the hands of innocent holders, see Parker *v.* Smith, 3 Bradw. (Ill.) 356.

[2] Foote *v.* Mt. Pleasant, 1 McCrary, 101.

[3] Leavenworth, L. & G. Ry. Co. *v.* Douglas Co., 18 Kans. 169. As to prescribing conditions of subscription and the effect upon the railroad company, see People *v.* Holden, 91 Ill. 446. Where the mere fact that a track was laid and trains run over it was not a compliance with the conditions upon which a subscription in aid of a railroad company was voted, as to its substantial completion before the bonds should be issued to it, see Memphis, Kansas & Colorado Ry. Co. *v.* Thompson, 24 Kans. 170.

the proceeds of the bonds to the construction of the road, has been held to have no application where the road had been completed before the bonds were delivered.[1]

§ 443. **When authority to subscribe to stock gives no power to issue bonds in payment.**— The effect of the statutes of Mississippi as to rendering aid to railroad companies by counties through which the railroads were to be built has been fully considered by the United States Supreme Court in a case coming before it. The court held that, under those statutes, there was no power in the county authorities to issue bonds in payment of subscriptions made by the county to the stock of such roads; that they could subscribe to the stock, but were limited, in payment of the same, to taxation as directed by the terms of the statute.[2]

[1] Breckenridge County *v.* McCracken, (1894) 61 Fed. Rep. 191. Bonds of an Illinois county held invalid for non-compliance with the conditions on which they were voted and issued in aid of a railroad company as to the time the road was to be completed, notwithstanding an extension of time for its completion had been granted by the County Court and board of supervisors, in German Sav. Bank *v.* Franklin County, 128 U. S. 526; s. c., 9 Sup. Ct. Rep. 159. See, also, Onstott *v.* People, 123 Ill. 489; Young *v.* Railroad Co., 75 Iowa, 140; Crane *v.* Railway Co., 74 Iowa, 330; Livingston County *v.* Bank, 128 U. S. 102.

[2] Wells *v.* Supervisors, (1880) 102 U. S. 625. Chief Justice WAITE, in delivering the opinion of the court, referred first to the powers of the county authorities under the statutes of the state generally, and the rulings in Beaman *v.* Leake County, 42 Miss. 247, and Hawkins *v.* Carroll County, 50 Miss. 762, and then said: "Undoubtedly section 17 authorized a subscription to the stock of the railroad company for the county, after a majority of the electors of the county had in the proper way given their consent, and it is possible, if there had been nothing more, that, under the rule of construction stated in Lynde *v.* The County, 16 Wall. 6, the subscription might have been paid in bonds. It seems to us, however, that the provisions of section 18 are such as to exclude any such presumption. By that section the boards of police (supervisors) were authorized to assess and collect a tax on the taxable property or the real property of the county, at their election, 'for the payment of the capital stock subscribed.' No other mode of payment was provided for. This, of itself, when considered in the light of the settled policy of the state, to require the current liabilities of counties to be discharged by current taxation, would seem to indicate an intention not to confer upon the counties the power of funding this kind of liability. But when it is taken in connection with the further provisions of the same section, which authorize the boards of police to direct that the railroad company issue to the taxpayers, in lieu of the county, stock to the amount of the taxes paid, the intention is even more apparent. As stock was to be issued by the county to an amount equal to the taxes paid, it would seem as though it could not have been sup-

A Missouri railroad company had a charter in which it was provided that, "upon the presentation of a petition of the president and directors of said company to the County Court of any county through which said road may be located, praying that a vote may be taken in any strip of country through which it may pass, not to exceed ten miles on either side of said road; that the inhabitants thereof are desirous of taking stock in said road and of voting upon themselves a tax for the payment of the same, it shall be the duty of said County Court to order an election therein,

posed that before the tax was collected any payment of the subscription was to be made, or any stock issued, that could in any manner interfere with this privilege of the taxpayers. So, too, the company could not be required to issue stock up and to the amount of the subscription. As the taxpayer was to be entitled to stock to the full amount of his payment, it follows that the tax must have been intended to pay the subscription and not bonds. We are not unmindful of the fact that the language of this part of the section is such as to leave it optional with the board to give this direction or not; that it may, nevertheless, be referred to, as we think, to strengthen the presumption arising from the other provisions, that the subscription was not to be paid through taxation, directly or indirectly, until the money to be raised in that way had actually been collected. This statute conferred an extraordinary power on the boards of police. It authorized them to create a new liability for their respective counties, and provided a special way of discharging that liability. The liability and the mode of discharge were provided for in the same statute. This being so, the mode prescribed is exclusive of all others. This case differs materially from Lynde *v.* The County, 16 Wall. 6. There the tax voted was to be levied annually during a period not exceeding ten years, and the amount for each year definitely fixed. As this was done for the purpose of building a court house, the court very properly held the vote implied permission to borrow money to accomplish the object in anticipation of the collection of the tax, which must necessarily be delayed a considerable number of years. Here the tax was to be levied to pay the subscription, that is to say, to pay the company the amount subscribed, when, by the terms of the subscription, that obligation was to be met. As the statute on its face contemplated no delay in raising the money by taxation, no implication of a power to borrow in anticition of the tax can arise. The subscription might be made, but the money must be raised by taxation to meet it. The railroad company cannot complain; for when it received the subscription it knew, or ought to have known, from what source the money was to come to meet the payment, and it impliedly gave its consent to such delays as were necessarily incident to the mode of collection. The other provisions of the charter as to calls on subscribers to meet their subscriptions were not necessarily applicable to counties. Counties were to pay as they agreed, and when the tax was collected. * * * From the supplemental act it is apparent that the object of the legislature was to raise money by taxation to aid in the construction of the road and require the company to give the taxpayers stock for the money they paid.

and shall prescribe the time, place and manner of holding said election; and if a majority of the taxable inhabitants shall determine in favor of the tax, it shall be the duty of said court to levy and collect from them a special tax which shall be kept separate from all other funds and appropriated to no other purposes, and as fast as collected shall cause the same to be paid to the treasurer of said company." An election was held in a strip of a county properly called by the County Court, and the vote was in favor of the subscription. The County Court subscribed to the stock of the company in obedience to the will of the people, and issued bonds in payment of the subscription. In an action upon the coupons of some of these bonds the Supreme Court held the bonds to be void, notwithstanding the suit was by a *bona fide* holder of the bonds, for lack of authority in the County Court to issue the bonds.[1]

§ 444. **When a donation of bonds is authorized.**— It was urged, against the validity of a particular statute of Nebraska,

This is entirely inconsistent with any idea of the payment of interest. As the special tax on adjoining lands was large, it was extended over a period of years. This amount was fixed and not left to the discretion of any one. In respect to the country at large the plan adopted was different. There it was left for the people to determine for themselves how much the subscription should be, and for the county and the company to agree when it should be paid. In this way the tax might be extended over a series of years; but as stock was to be issued by the company for all payments made, it could not have been intended to tax beyond the actual amount of the subscription. Consequently, if time was given by the company to make the payment, it must be without interest."

[1] Ogden *v.* County of Daviess, (1883) 102 U. S. 634; followed in Deland *v.* Platte County, (1890) 54 Fed. Rep. 823, in which case this question and others pertinent to it are fully discussed by PHILLIPS, D. J. In Ogden *v.* County of Daviess, *supra*, referring to the provision of the charter above referred to, WAITE, Chief Justice, for the United States Supreme Court, said: "Without doubt [this provision of the charter] authorized the taxable inhabitants of the 'strip of country' designated to vote a tax upon themselves to take stock, and required the County Court to levy and collect such a tax, if voted, and pay over the money as fast as collected to the treasurer of the company; but in this we find no authority for the county to issue bonds in anticipation of the tax. The taxable inhabitants of the strip of country could not themselves make a bond, and all the County Court could do was to collect and pay over the tax voted. The inhabitants were not even organized by themselves, much less made a body politic for any purpose. They could vote the tax if called upon to do so by the County Court, but that was all. The effect of the vote was nothing more than to authorize the County Court to levy, collect and pay over to the treasurer of the company the

that it authorized the donation of the county bonds to the railroad company, and it was insisted that if even the legislature could empower the county to subscribe to the stock of such a corporation, it could not constitutionally authorize a donation. The United States Supreme Court sustained the constitutionality of the statute.[1] The Nebraska Supreme Court has held that

special tax they had determined upon."

[1] Railroad Company *v.* County of Otoe, (1872) 16 Wall. 667; cited and applied in Otoe County *v.* Baldwin, (1884) 111 U. S. 1. Mr. Justice STRONG, *arguendo*, said: "There is no solid ground of distinction between a subscription to stock and an appropriation of money or credit. Both are for the purpose of aiding in the construction of the road; both are aimed at the same object, securing a public advantage, obtaining a highway or an avenue to the markets of the country; both may be equally burdensome to the taxpayers of the county. The stock subscribed for may be worthless, and known to be so. That the legislature of the state might have granted aid directly to any railroad company by actual donation of money from the treasury will not be controverted. No one questions that in the absence of some constitutional inhibition the power of a state to appropriate its money, however raised, is limited only by the sense of justice and by the sound discretion of its legislature. If the power to tax be unrestricted, the power to appropriate the taxes is necessarily equally so. Accordingly, nothing has been more common in the state and federal governments than appropriations of public money raised by taxation to objects, in regard to which no legal liability has existed. State legislatures have made donations to numerous purposes whenever, in their judgment, the public well-being required them, and the right to make such gifts has never been seriously questioned. But if a state can directly levy taxes to make donations to improvement companies, or to other objects which, in the judgment of its legislature, it may be well to aid, it will be found difficult to maintain that it may not confer upon its municipal divisions power to do the same thing. Counties, cities and towns exist only for the convenient administration of the government. Such organizations are instruments of the state, created to carry out its will. When they are authorized or directed to levy a tax, or to appropriate its proceeds, the state, through them, is doing indirectly what it might do directly. It is true the burden of the duty may thus rest upon only a single political division, but the legislature has an undoubted power to apportion a public burden among all the taxpayers of the state, or among those of a particular section. In its judgment, those of a single section may reap the principal benefit from a proposed expenditure, as from the construction of a road, a bridge, an almshouse or a hospital. It is not unjust, therefore, that they should alone bear the burden. This subject has been so often discussed, and the principles we have asserted have been so thoroughly indicated, that it seems to be needless to say more, or even to refer at large to the decisions." These few cases were cited: Blanding *v.* Burr, 13 Cal. 343; Town of Guilford *v.* Supervisors of Chenango County, 3 Kern. 149; Stuart *v.* Supervisors, 30 Iowa, 9; Augusta Bank *v.* Augusta, 49 Me. 507. As to the objection that the road

bonds issued by a county as a donation to a railroad company were invalid unless they had indorsed upon them a certificate signed by the secretary and auditor of state, showing that they were issued pursuant to law.[1]

§ 445. **When county bonds donated to a railroad company cannot be scaled down.**— The holders of some of the bonds of Dixon county, Nebraska, issued as a donation to a railroad company, brought their bill in equity in the United States Circuit Court for that district for relief. The court held that these bonds having been held void in a court of law as in excess of the constitutional limit of indebtedness, equity had no power to scale down the issue to the limit and enforce it against the county, the contract being indivisible and void *in toto*, and there being no executed consideration to support an implied promise.[2] There was an appeal from this judgment rendered by BREWER, Circuit Judge, to the United States Supreme Court, where the judgment was affirmed.[3]

aided lay outside the limits of the county, and outside the state, it was said: "There is nothing in this objection. It was for the legislature to determine whether the object to be aided was one in which the people of the state had an interest, and it is very obvious that the interests of the people of Otoe county may been more involved in the construction of a road giving them a connection with an eastern market than they could be in the construction of any road wholly within the county. But that the objection has no weight may be seen in Gelpcke *v.* Dubuque, 1 Wall. 175, and in Walker *v.* Cincinnati, 21 Ohio St. 14."

[1] State *v.* Roggen, 22 Neb. 118; s. c., 34 N. W. Rep. 108.

[2] Hedges *v.* Dixon County, (1889) 37 Fed. Rep. 304.

[3] Hedges *v.* Dixon County, (1893) 150 U. S. 182. The subject is so fully discussed by the majority of the Supreme Court that the opinion is deemed worthy of reproduction here. Mr. Justice JACKSON, for the majority of the court (HARLAN, J., only dissenting), said: "The bonds in question were made payable to the [railroad company, the donee], or bearer, and were put in circulation by that company with its indorsement thereon, guaranteeing to the holders the payment of the principal and interest of the bonds, according to the tenor thereof, at the place where, and as they became due and payable. The only consideration received by the county in the transaction was the incidental benefit derived from the construction of the railroad — the proceeds of the bonds, when negotiated, being received directly by the railroad company. The theory of the bill is that the bonds are void only to the extent that they exceed ten per cent of the assessed valuation of the property of the county at the time of their issuance, and upon the abatement of that excess the holders are entitled to have the residue thereof — which the county could have lawfully issued — treated as valid because of the incidental ben-

§ 446. **Bonds of an Illinois county secured by mortgage of its swamp lands.**—The charter of an Illinois railroad company provided in one section that "The corporation may borrow such sums of money as they deem advisable, and upon such terms as they may agree, for the carrying out of the objects of this act, and may provide any security therefor they think best by bond and mortgage." In another section it empowered the County Court of the county in which was its starting point to subscribe for its stock, to issue bonds of the county and provide for the payment of the principal and interest thereof by *sale* or *mort-*

efits derived from the construction of the road which was sought to be secured by the donation of bonds. The complainants, by their bill and exhibit thereto, have presented the same state of facts which were considered in Dixon County *v.* Field, 111 U. S. 83, where the bonds in question were directly involved, and were held by this court to be void because they exceeded in the aggregate the sum of ten per cent of the assessed valuation of the property of the county at the time of their issue. This decision was based upon [that section] of the Constitution of the state of Nebraska which provides as follows: 'No city, county, town, precinct, municipality, or other subdivision of the state, shall ever make donations to any railroad or other work of internal improvement, unless a proposition shall have been first submitted to the qualified electors thereof at an election by authority of law; *Provided*, that such donations of a county, with the donations of such subdivisions, in the aggregate shall not exceed ten per cent of the assessed valuation of such county.' While the complainants concede that the issue of bonds was in excess of what the county was authorized to donate under the provision of the Constitution, and for that reason were invalid at law, they insist that a promise to pay so much thereof as could have been lawfully issued shall be implied and enforced against the county, under the principle applied in Louisiana *v.* Wood, 102 U. S. 294, and in Read *v.* Plattsmouth, 107 U. S. 568. Those cases are clearly distinguishable from the present. In Louisiana *v.* Wood, by the act of the city, the bonds bore a false date which, apparently, made them obligatory and binding; they were sold by the city and purchased by the holders in good faith, and the money paid for them went directly into the city's treasury. This court held that the city was in the market as a borrower and received the money in that character, notwithstanding the transaction assumed the form of a sale of her securities, which, being defectively executed, a suit could not be maintained thereon, and that the holder was entitled to recover the money paid with interest thereon from the time the obligation of the city to pay was denied. In Read *v.* Plattsmouth the bonds were issued by a city for the purpose of raising money wherewith to construct a high school building within her limits. The bonds were sold and the proceeds applied to that purpose. The legislature subsequently legalized the proceedings of the city in the premises, but this act of the legislature was passed after the Constitution of the state went into effect declaring that the 'legislature shall pass no special act conferring corporate powers,' and that 'no bill

gage, one or both, of the *swamp* and *overflowed lands* of such county, and dispose of such bonds for money to pay or in payment of their subscription to said stock, all and each to be upon such time, *terms* and in such *mode* as they may deem best; or they *may make such other disposition* of said swamp and overflowed lands in *aid* of the *construction* and maintenance of said railroad as they *deem best* for the public interest of said county. Another section provided for the submission to the voters of the county propositions looking to the carrying out of the purposes of the charter provisions. There was an additional section in

shall contain more than one subject, which shall be clearly expressed in its title.' A purchaser of the bonds for value, without notice of any infirmity in their issue, brought suit to recover the amount of the coupons then due and unpaid. It was held that as, by force of the transaction, the city was bound to refund the moneys paid it in consideration of its void bonds, and as the act, by confirming them, merely recognizes the existence of that obligation and provides a medium for enforcing it according to the original intention of the parties, no new corporate powers were thereby conferred. In this case, as in Louisiana *v.* Wood, the city got the full pecuniary consideration for the bonds and applied the money for the very purpose for which they were issued; and, upon well-settled principles, if the securities given for the money so obtained proved invalid or defective for any reason, there was a clear legal as well as moral obligation to refund the money which had been so advanced to and received by the city. The circumstances and conditions which gave the holders of the bonds an equitable right in those cases to recover from the municipality the money which the bonds represented do not exist in the case under consideration, where the county received no part of the proceeds of the bonds and no direct money benefit, but merely derived an incidental advantage arising from the construction of the railroad, upon which advantage it would be impossible for the court to place a pecuniary estimate or to say that it would be equal to such portion of the bonds in question as the county could lawfully have issued. Moreover, by the provisions of the Constitution of the state of Nebraska, and by the express terms of the proposition submitted to the vote of the people of Dixon county, the bonds in question were issued *as a donation to the railroad company*, and, being intended as a donation, it cannot properly be said that the purchasers of these bonds from the railroad company paid any consideration therefor to the county so as to raise any equity as against it for the amount represented by the bonds or any part thereof. Any equitable demand which might under the circumstances have existed against the county on the theory of consideration received, was in favor of the railroad company which constructed the railroad, and thereby conferred all the incidental benefits which the county derived from the transaction. If any equitable claim arises in favor of the holders of the bonds, it must be against the railroad company from whom the bonds were purchased and by whom their payment was guaranteed, as that company was the recipient of the legal consideration realized upon the nego-

these words: "Any county through which said road *may* run, and *every* county through which *any other railroad may* run with which this road *may be joined*, *connected* or *interested may*, and are hereby *authorized* and *empowered* to, *aid* in the *construction* of the *same*, or of *such other road* with which it may so connect; and for this purpose the provisions [above referred to] *shall extend*, *include* and be *applicable* to *every* such county and *every such* railroad." A county through which this road finally was to run, itself or by connection with another, through its county officials, executed a mortgage of its swamp lands to a

tiation of the bonds. Again, the Constitution of the state having prescribed the amount which the county might donate to a railroad company, that provision operated as an absolute limitation upon the power of the county to exceed that amount, and it is well settled that no recitals in the bonds or indorsed thereon could estop the county from setting up their invalidity based upon the want of constitutional authority to issue the same. Recitals in bonds issued under legislative authority may estop the municipality from disputing their authority as against a *bona fide* holder for value; but when the municipal bonds are issued in violation of a constitutional provision, no such estoppel can arise by reason of any recitals contained in the bonds. Lake County *v.* Rollins, 130 U. S. 662; Lake County *v.* Graham, 130 U. S. 674; Sutliff *v.* Lake County Commissioners, 147 U. S. 230. But, aside from this view of the subject, the bill proceeds upon the false assumption that the bonds in question were partly valid and partly void, and that the case is brought within the principle announced in Daviess County *v.* Dickinson, 117 U. S. 657. In that case, under authority conferred by statute, the county voted a subscription of two hundred and fifty thousand dollars to a railroad company, which was made, and, by order of the County Court, bonds of the county to that amount were ordered to be sold and disposed of by a committee for the purpose of paying such subscription. The officers of the county, without authority, executed and issued bonds in the amount of three hundred thousand dollars. The bonds, as they were delivered, were separately numbered and entered upon the county register. The court held that the power to issue bonds was limited to two hundred and fifty thousand dollars, and that the bonds issued in excess of that amount were unlawful and void. It was further held that bonds to the amount authorized, which were first issued and delivered, were valid and entitled to payment. In that case there was a clear and well-defined line between the legal and illegal issues which enabled the court to declare invalid such of the bonds as exceeded the amount authorized and to hold that the illegal excess did not vitiate the bonds which were authorized and legally issued. There was no scaling of the entire issue in that case so as to bring it within the limits of the county's authority. The two hundred and fifty thousand dollars, which the court pronounced valid, had been expressly authorized by the county, and the bonds for that amount were readily separated from the fifty thousand dollar excess which had not been authorized. It did not, therefore, involve any investigation on the part of the court to ascertain what the county could lawfully issue, but was

trustee, as a security for bonds of the railroad company which it had resolved to issue to a certain amount upon which to borrow money to construct its road under the authority given in the above provisions of the charter of the railroad company in aid of its construction. In an action to foreclose the mortgage upon these lands in behalf of the bondholders, the county resisted and the bill for foreclosure was dismissed upon the ground that the proofs failed to show that at the date of the mortgage and deed of trust for securing the payment of the bonds there was any line of railroad constructed, or authorized to be constructed, through

merely the identification of the bonds which it intended to issue. Again, the amount of the bonds issued was not based upon the assessed valuation of the property of the county, but was limited to the amount which the people of the county, by an election held, had determined should be issued. There is a radical difference in these respects between that case and the one under consideration. What the county authorized and carried into execution in the present case, both by the vote and by the donation, was one entire transaction, and if it should be so reformed as to curtail the entire issue of bonds to such an amount as was within the constitutional limits of the county to donate, it would be something different from that which was voted by the county and carried into effect by the issue of the bonds. This would involve the making of a different donation from what the county voted and intended to make to the railroad company. It is urged that the vote and the issue of the bonds constituted a contract between the railroad company and the county, and that the bonds issued in pursuance thereof should be scaled, as sought by the bill, to bring the contract within the authority of the county; that as the county intended to make a valid donation such reduction of the amount of the issue which the complainants offer to make should be sanctioned by the court and the residue declared valid. But the difficulty in the way of this suggestion is that, treating the transaction as a contract, it is not within the power of a court of equity to change its terms and provisions. Besides, it is not shown that the county would have voted a different amount from what was issued, or that it intended to issue a less amount. It is too well settled to need citation of authorities that a court of equity, in the absence of fraud, accident or mistake, cannot change the terms of a contract. Again, if a right to the equitable relief sought by the complainants could be worked out on the theory of a contract between the county and the railroad company, it would be necessary to establish that such a contract actually existed and was valid. In the present case, however, the county had no authority to vote the donation. In Reineman *v.* Covington, Columbus & Black Hills Railroad, 7 Neb. 310, where an excessive issue of bonds had been voted by the county in aid of internal improvements, it was held by the Supreme Court of Nebraska that the vote was simply a void act, and conferred no authority on the county officials to issue the bonds of the county, either to the amount voted or for any amount. It was urged in that case, as in this, that even if it should be held that the proposition submitted to the electors was in excess of the amount

the county defendant with which the bonded railroad was joined, connected or interested. Upon appeal, the Supreme Court of the United States held that the section of the charter last referred to, upon the authority of which the mortgage was executed, did not require that the road to be aided should be actually built before a county was authorized to mortgage its lands, but contrariwise, that the aid was intended to be given before the road was built, and that the counties giving the aid were expected to take the ordinary risk of the success of the undertaking in which they embarked their property. Further, they held that where another

authorized to be voted, still, to the extent that the county could have lawfully voted and issued such bonds, they should be treated as constituting a contract between the county and the railroad company, and to that extent be upheld. The Supreme Court of the state declined to accede to this view of the subject, and ruled that 'the proposition submitted to the electors was an entirety and indivisible. It exceeded the statutory limit, and was, therefore, wholly unauthorized. The election was simply a void act, conferring no authority whatever upon the county commissioners to issue bonds of the county in any manner whatever.' Several state decisions have been cited in support of the bill: Johnson *v.* County of Stark, 24 Ill. 75; City of Quincy *v.* Warfield, 25 Ill. 317; Briscoe *v.* Allison, 43 Ill. 291; State *v.* Allen, 43 Ill. 456; Stockdale *v.* Wayland School District, 47 Mich. 226. But they mostly relate to taxes imposed beyond authority, and stand upon a different doctrine from that involved in the present case. We do not, however, deem it necessary to review them, for if they can be construed to support a bill like the one under consideration, we think they are not founded upon correct principles, and are not in harmony with the decisions of this court." Then there was the following comment upon certain of the cases adjudicated in this court: "In Buchanan *v.* Litchfield, 102 U. S. 278, bonds were issued by the city of Litchfield, under authority of a statute of Illinois and an ordinance of the city, for the construction of a system of water works for the use of the municipality. Neither the statute nor the ordinance contained any reference to the provisions of the Constitution prohibiting any county, city, township or school district from becoming indebted in any manner, or for any purpose, to an amount, including exisiting indebtedness, in the aggregate exceeding five per cent of the taxable property therein. The ordinance of the city made no reference to or mention of the indebtedness of the city, although at that time it exceeded the constitutional limit. A *bona fide* holder of the bonds brought suit upon the unpaid coupons thereto attached, and it was held that they were void and could not be recovered. In this case the city was directly benefited by the issue of the bonds, which were negotiated for the sole purpose of erecting a system of public works. The holders of the bonds thereafter sought relief by a bill in equity against the city of Litchfield to enforce the payment of the money loaned, or which the city had received upon the bonds and used in the construction of its public works. The question of their right to recover on the equitable consideration came before this court

company was subsequently chartered to build a road, the course of which ran up to one terminus of the road of the company previously chartered, and thence onward completely through another county adjoining the county in which the former road lay, and the railroad company first chartered undertook the construction of the new road from the terminus above mentioned onwards, completely through the other and adjoining counties, that the authority to construct the connecting road and the entering into a contract for its construction formed a "connection" within the meaning of this provision of the charter.[1]

in Litchfield *v.* Ballou, 114 U. S. 190, and it was held that a provision in a State Constitution that a municipal corporation shall not become indebted in any manner, and for any purpose, to an amount exceeding five per cent of its taxable property therein, forbids implied as well as express liability for the amount or amounts received on bonds issued contrary to such provision, and that a court of equity could not afford relief in such a case either as an express or implied obligation; that the transaction being invalid at law was equally invalid in equity. This conclusion was reached after a free review of the authorities on the question, and the court denied the relief sought. In Ætna Life Insurance Co. *v.* Middleport, 124 U. S. 534, the town of Middleport made an appropriation to a railroad company, to be raised by tax on the property of the town, and bonds of the town for a sum large enough to include interest and discount for which they could be sold and delivered were issued to the railroad company, by whom they were put in circulation. These bonds were declared void, and the insurance company, as a purchaser and holder for value and without notice, of a portion thereof, sought by a proceeding in equity to be subrogated to the rights of the railroad company to enforce payment of the amount of the appropriation voted by the town; but it was held that the purchase of these bonds by the holder was no payment of the appropriation voted by the town, and that the holder was not entitled to claim the benefit of such appropriation, nor that the advantages conferred by the railroad company upon the town inured to the benefit of the holder, or constituted the basis of a consideration on which it could claim to be paid the sum appropriated for the railroad company. The proposition contended for in that case by the complainant was that by its purchase of the bonds, which were supposed to represent the benefit conferred upon the town by the appropriation to the railroad company, it became entitled in equity to claim the payment of the amount represented by the bonds on the basis of the original consideration. This contention was not sustained, and the complainant was denied the equitable relief sought. The principle running through these decisions controls the case under consideration, and clearly establishes that the complainants are not entitled to the relief they seek. The fact that the complainants have no remedy at law, arising from the invalidity of the bonds, confers no jurisdiction upon a court of equity to

[1] Kenicott *v.* Supervisors, (1872) 16 Wall. 452.

§ 447. **Precinct aid bonds.**— The charter of a railroad company of Kentucky provided that any county through which it might pass, or any magisterial precinct or precincts of such county, might subscribe to its capital stock; that, when any precinct or precincts made such subscription, bonds of the county should be issued, showing on their face the precincts making the subscription, which alone should be bound to pay the bonds. A defined portion of a certain precinct in a county named was excepted from the provisions of the act. The residue of that precinct joined with another precinct of the county in making a subscription, and the bonds issued by the county for these subdivisions were the ones involved in this action. The United States Circuit Court of Appeals for the sixth circuit held that there was power in the residue of that precinct not excepted to join with another in making this subscription and the joint bonds were properly issued therefor. The same charter provided that such subscriptions should be paid by taxes levied in such precincts alone. The appellate court held that the assessor for the payment of the bonds involved in the suit might be required to list separately the property of the district making such subscription, and liable to a tax therefor under the statutes of Kentucky which require him to make separate books for each "taxing district of his county, by wards or other subdivisions, as convenience may require."[1]

afford them relief. The established rule, though not of universal application, is that equity follows the law, or, as stated in Magniac *v.* Thomson, 15 How. 281, 291, 'that whenever the rights or the situation of parties are clearly defined and established by law equity has no power to change or unsettle those rights or that situation, but in all such instances the maxim *equitas sequitur legem* is strictly applicable.'"

[1] Breckenridge County *v.* McCracken, (1894) 61 Fed. Rep. 191. There was an objection on the part of the county that no power was conferred to assess a tax upon either the interest or principal of the bonds to be issued, and that, therefore, no authority to issue the bonds or subscribe for the stock had been conferred. LURTON, Circuit Judge, upon this objection, said: "To support this proposition counsel rely upon a doctrine to that effect in Kentucky Union R. Co. *v.* Bourbon Co., 85 Ky. 111; s. c., 2 S. W. Rep. 687. The same principle was laid down by Justice MILLER in Citizens' Savings & Loan Assn. *v.* City of Topeka, 20 Wall. 660, where it was said that 'the validity of a contract which can only be fulfilled by a resort to taxation depends on the power to levy the tax for that purpose.' The language was applied in a case where the validity of bonds issued by the city of Topeka to aid a private manufacturing establishment was in question. The court said, as

§ 448. **The denomination of bonds changed from those named in the proposal under Alabama statutes — their validity not affected thereby.**— The bonds from which the coupons upon which these actions were brought were detached, were issued in Alabama in sums of a different denomination from those named in the proposal of a railroad company receiving them, made to the county authorities under the statutes of that state relating to aid bonds. The validity of the bonds was questioned before the United States Supreme Court on account of this variance. Section 11 of the act under which the bonds were issued provided "that the bonds shall be of such denomination as the Court of County Commissioners and said railroad company may agree upon, but not to be for less than one hundred dollars nor more than one thousand dollars." In the proposition of the company to Greene county it was suggested that the bonds to be issued in payment of the subscription should be "in the sum of

such bonds could only be paid by taxation they were void unless taxes might be constitutionally levied for the purpose of aiding a purely private enterprise. Here we have no such question, for, under the Constitution of Kentucky, taxes may be levied to aid a railway line, it being deemed a public enterprise. There can be in this case no serious doubt but that the power to assess a special tax upon the property of the affected district has been conferred on the County Court of Breckenridge county for the purpose of paying off the interest and principal of these bonds. Section 14 of the charter provides that 'an annual tax sufficient to pay the semi-annual installments of interest on such bonds, and the principal when it shall become due, shall be collected and paid out by the officers of such counties, cities or towns, as provided in the case of other county, city or town taxes.' The criticisms on this provision are (1) that no means are provided, and none existed before, for ascertaining the amount of taxable property in the unorganized district; (2) that in attempting to confer the taxing power it does so by referring to a criterion which has no existence in law. We think these objections quite untenable. The power to assess, levy and collect a tax would be necessarily implied from the power to create the debt, there being nothing in the act indicating an expectation that payment should be made in any other way, and no constitutional obstacle, either in the character of the debt or to the granting of such power by the legislature, being suggested. Citizens' Savings & Loan Assn. *v.* City of Topeka, 20 Wall. 656; Ralls Co. *v.* U. S., 105 U. S. 735; Quincy *v.* Jackson, 113 U. S. 335; s c., 5 Sup. Ct. Rep. 544. The purpose that this debt shall be paid by taxation is made clear. That no general authority exists to levy an *ad valorem* tax for general county purposes is not important. The power to assess and levy a special *ad valorem* tax is by implication clearly conferred in section 14, to say nothing of the implication which results from the grant of power to create the debt and then the bonds."

one and five hundred thousand dollars each." In the records of the court ordering the election the proposition, as recorded, was that the bonds be "in the sum of one thousand five hundred dollars each." The final action of the court was to issue bonds of $500. In the Pickens County case the proposition was that the bonds be in the sum of $1,000 each, but after the election, with the consent of the company, it was ordered by the court that one-half the amount should be in the sum of $250, and the other half $1,000, and the bonds actually put out were of these denominations. The court sustained the validity of the bonds over this objection.[1]

§ 449. **What amounts to a gift of bonds in aid not authorized.**—A statute of Illinois incorporating a railroad company empowered municipal corporations, when authorized by popular vote, to subscribe for stock in the company and issue bonds in payment therefor. A county agreed, by popular vote, to subscribe for $100,000 of stock and issue bonds therefor, but before issuance of the bonds the county authorities agreed to sell the stock back to the company in exchange for $5,000 in bonds. In fact, only $95,000 of bonds were issued and delivered to the company and no stock received by the county. The United States Circuit Court of Appeals for the seventh circuit held that the bonds were void, as the transaction, being a gift and not a subscription, was not authorized by the statute nor assented to by the popular vote.[2]

[1] County of Greene *v.* Daniel, (1880) 102 U. S. 187; County of Pickens *v.* Daniel, (1880) 102 U. S. 187. Chief Justice WAITE, for the court, said: "As to the Greene County case, it is apparent that there was a clerical mistake, either in the proposal or the record, as to the description of the bonds to be issued, and it is easy to see that the intention was to have bonds of a thousand dollars and five hundred dollars each, but in the Pickens County case the proposition was distinctly that they should be for one thousand dollars. This, however, we consider unimportant, for section 11 expressly provides for bonds of such denomination as the Commissioners' Court and the company should agree on. From this it is clear that the parties were not bound in this particular by the sums specified in the proposal. They were limited by the proposition as accepted in respect to the total amount of the issue, but not the denomination. The bonds as issued were of such denominations as the law allowed the court and the company to agree on, and that, in our opinion, is enough."

[2] Post *v.* Pulaski County, (1892) 49 Fed. Rep. 628. BLODGETT, D. J., said: "No special or general statute of the state then in force authorized the county to make a donation of its money or bonds in aid of this railroad

§ 450. **Consolidation of railways — effect as to county aid.** — In an action by a railroad company against the county commissioners of an Indiana county, praying that there be awarded to them, by way of subrogation, a sum of money which had been, as alleged, awarded in aid of certain railroad companies, these rules were declared: A general statute authorizing the consolidation of railroad companies must be considered a silent factor in a subsequent contract of subscription made by a township to the stock of a railroad company, and a consolidation of such company with another company will not release the township, but will transfer its obligation to the new company. In Indiana a mere vote by a township of a given sum in aid of a railroad gives the company no legal right to or interest in the tax until the same has been levied and collected, and a valid contract of subscription made in behalf of the township. And if it be conceded that such

company. That there is an essential difference between a proposition to subscribe for stock in a railroad company, and thereby become a stockholder, with a right to share in the profits of its business and have a voice in the management and policy of the company, and a proposition to make a donation of bonds or money to the railroad company is too plain to require argument or the citation of authority. The order of the County Court, making the subscription to the stock and directing the issue of the bonds, and which must be read into each bond and coupon, shows in unmistakable language, so plain that it requires no technical skill to construe or apply it, that the bonds were issued as a donation to the railroad company and not in payment of a subscription to its stock. The case of Choisser *v.* People, 140 Ill. 21; s. c., 29 N. E. Rep. 546, lately decided by the Supreme Court of Illinois, * * * is almost identical in its facts, as far as the questions now under consideration are concerned, with this case. It involved an issue of bonds by another county (Saline) in aid of the construction of the same railroad, and in pursuance of the same section of the charter of the railroad company. An agreement between that county and the railroad company was made after the vote authorizing the subscription, in substantially the same terms as was made in the case now under consideration. And in that case the court, speaking by Mr. Justice Bailey, said, in regard to this contract: 'That in its consummation, if not in its inception, the transaction was a donation, pure and simple, is too plain to admit of serious controversy. In the beginning, and until the election was had, the guise of a subscription was resorted to so as to bring the municipal aid sought to be obtained apparently at least within the power conferred upon the county by the tenth section of the railroad company's charter. But, when viewed in the light of the interpretation put upon the transaction by the subsequent acts of the parties, it appears too transparent to mislead. The bonds being essentially a donation, it was not within the power of the County Court to issue them, and they must, therefore, be held to be *ultra vires* and void.'"

a vote gives a contingent interest which will pass to a new company by consolidation, such new company cannot assert any claim to the fund when it has not tendered the stock therefor, and has no stock which it may legally tender.[1] A township of Missouri having subscribed in aid of a railroad company, a Missouri corporation, under the laws of that state, by a vote, which railroad company, under a statute authorizing it, was afterwards consolidated with a railroad company which was an Iowa corporation, and the bonds were subsequently issued to the latter, upon the question of the effect of the consolidation and the rights of the parties involved, the Supreme Court of the United States sustained the validity of the county bonds issued on behalf of the township. They held that the consolidation was authorized, and the right to receive the subscription passed to the consolidated company; further, that the vote on the subject of the subscription contemplating the construction of the railroad which the consolidated company built, there was no diversion from the purpose contemplated by the vote, in the fact that the stock was subscribed and the bonds issued to the consolidated company.[2] In a case where the Supreme Court of the United States held that a subscription of stock and issue of county bonds, authorized upon a vote of the people of the county to the original corporation, could not be legally made to one of the three new corporations into which, by an amendatory act, the legislature of Illinois had divided the original corporation, it was contended that the plain-

[1] Pope *v.* Board of Comrs. of Lake County, (1892) 51 Fed. Rep. 769, in which the court overruled the demurrer to the intervening petition of the townships and a taxpayer asserting their rights to the fund. See Board Comrs. Hamilton Co. *v.* State, 115 Ind. 64; s. c., 4 N. E. Rep. 589, and 17 N. E. Rep. 855; Centre Township *v.* Board, etc., 70 Ind. 562, as to the rights of the township where the right of the railroad to aid has never existed, or has ceased to exist.

[2] Livingston County *v.* First National Bank of Portsmouth, (1888) 128 U. S. 102. Mr. Justice BLATCHFORD, in the opinion rendered in this case, reviews at length the following cases involving consolidation of the companies to which aid is voted with other companies, and under other names: County of Scotland *v.* Thomas, 94 U. S. 682; Town of East Lincoln *v.* Davenport, 94 U. S. 801; Wilson *v.* Salamanca, 99 U. S. 499; Menasha *v.* Hazard, 102 U. S. 81; Harter *v.* Kernochan, 103 U. S. 562; New Buffalo *v.* Iron Company, 105 U. S. 73; Nugent *v.* The Supervisors, 19 Wall. 241; Empire *v.* Darlington, 101 U. S. 87; County of Tipton *v.* Locomotive Works, 103 U. S. 523. He commented, also, upon County of Bates *v.* Winters, 97 U. S. 83; Bates County *v.* Winters, 112 U. S. 325; Harshman *v.* Bates County, 92 U. S. 569.

tiff was an innocent purchaser of the bonds without notice of their invalidity. Mr. Justice FIELD, speaking for the court, said: "If such were the fact we do not perceive how it could affect the liability of the [county issuing the bonds]. This is not a case where the party executing the instruments possessed a general capacity to contract, and where the instruments might, for such reason, be taken without special inquiry into their validity. It is a case where the power to contract never existed — where the instruments might, with equal authority, have been issued by any other citizen of the county. It is a case, too, where the holder was bound to look to the action of the officers of the county and ascertain whether the law had been so far followed by them as to justify the issue of the bonds. The authority to contract must exist before any protection, as an innocent purchaser, can be claimed by the holder. This is the law even as respects commercial paper, alleged to have been issued under a delegated authority, and is stated in the case of Floyd Acceptances, 7 Wall. 676." In speaking of notes and bills issued or accepted by an agent, acting under a general or special power, the court says: "In each case the person dealing with the agent, knowing that he acts only by virtue of a delegated power, must, at his peril, see that the paper on which he relies comes within the power under which the agent acts. And this applies to every person who takes the paper afterwards; for it is to be kept in mind that the protection which commercial usage throws around negotiable paper cannot be used to establish the authority by which it was originally issued."[1] A county of Tennessee, lawfully authorized to issue its bonds in payment of a subscription to a railroad corporation of that state, through its County Court subscribed to the stock and issued its bonds and delivered them to the corporation. Between the Tennessee railroad company and another, a Kentucky corporation, a consolidation was about to take place. Before this step was taken the Kentucky company, through its agent, submitted the following proposition to the County Court, which represented the county issuing the bonds, to wit: "That this company will grant an extension of time for the payment of said bonds and interest, so that the said payments shall be extended to the period of ten years from the date of the bonds, in ten annual installments, instead of the time

[1] Marsh *v.* Fulton County, (1870) 10 Wall. 676, 683.

they now have to run; this extension to apply to all bonds which this company owns or controls. But this proposition should be made a condition that the County Court of [the county issuing the bonds] shall immediately levy a tax and proceed to its collection, for the amount now due under this offer, and that they shall each year levy, collect and promptly pay over the amount to fall due each year, as the same falls due, during the whole period of this proposed extension; and in case of failure to levy, collect, or promptly pay over said annual amount, then the remaining bonds to become due, according to their original terms." The County Court, it appeared, accepted this proposition and the two roads were consolidated under another name, and under the control of the Kentucky corporation the road was constructed through the Tennessee county and to its final terminal point in that state. These bonds were used by the consolidated company for the purposes of this construction and the equipment of the road, and in due course of trade, for value, and in good faith, passed to the holder who brought an action upon them, the county claiming as a defense that there was fraud and collusion in the procuration of and issue of the bonds originally to the Tennessee company and that they were void for that reason. The United States Supreme Court held that there was no error in the instructions of the Circuit Court to the jury on the trial of the case, and that the county was estopped from denying the validity of the bonds in the hands of a *bona fide* holder, to whom they were transferred for value by the consolidated company.[1] The line of a consolidated railroad corporation, when completed according to its charter, must form a continuous track with those of the other constituents of the consolidated corporation, so as to admit of the passage of trains without break or interruption before the power of one of the constituent corporations to acquire land in aid of the construction of its road will pass to the consolidated corporation.[2]

§ 451. Constitutionality of a Tennessee aid statute.— The general statute of Tennessee required the County Courts, when thereunto authorized by a popular vote at an election held for the purpose, to subscribe for stock in a railroad company. A

[1] County of Tipton *v.* Locomotive Works, (1880) 103 U. S. 523.

[2] Georgia Pac. Ry. Co. *v.* Gaines, 88 Ala. 377; s. c., 7 So. Rep. 382, following Railway Co. *v.* Wilkes, (Ala.) 6 So. Rep. 34.

special statute was subsequently passed, which, without requiring the submission of the question of subscription to a popular vote, conferred power on the County Courts of the counties on the line of a particular railroad to make, and on the company to receive, a subscription of its stock. In an action upon bonds issued under this last act, it was contended that the last-mentioned statute was in violation of the Constitution of the state of Tennessee. The United States Supreme Court sustained the constitutionality of the statute.[1]

§ 452. **Ratification of bonds.**—There was in a case before the United States Supreme Court also this contention, that if the bonds in suit were issued without authority their issue was subsequently ratified, and various acts of the supervisors of the county were cited in support of the supposed ratification. To this it was said by the court: "These acts fall very far short of showing any attempted ratification even by the supervisors. But the answer to them all is that the power of ratification did not lie with the supervisors. A ratification is, in its effect upon the act of an agent, equivalent to the possession by him of a previous authority. It operates upon the act ratified in the same manner as though the authority of the agent to do the act existed originally. It follows that a ratification can only be made when the party ratifying possesses the power to perform the act ratified. The supervisors possessed no authority to make the subscription or issue the bonds in the first instance without previous sanction

[1] County of Tipton *v.* Locomotive Works, (1880) 103 U. S. 523. The court considered the effect of the rulings in all the cases before the Tennessee court, with an elaborate discussion of the principal cases, and Mr. Justice HARLAN, speaking for the court, said: "Looking, then, as well at the language of the Constitution [of Tennessee, 1834] as at the course of decision in the Supreme Court of Tennessee up to the time the acts of 1867 and 1869 were passed, and giving full effect to its latest utterance, to which our attention has been called, and remembering, also, that the power given to a municipal corporation to subscribe to the stock of a railroad company may be, also, a right and privilege of that company (County of Scotland *v.* Thomas, 94 U. S. 682; Wilson *v.* Salamanca, 99 U. S. 499; Empire *v.* Darlington, 101 U. S. 87, 91), our conclusion is that those acts were not repugnant to the Constitution of the state, by reason of the authority they confer on a limited number of counties to make, and on a particular railroad corporation to receive, a subscription of stock, nor because they dispensed with the previous assent of the people of such counties expressed at a popular election."

of the qualified voters of the county. The supervisors in that particular were the mere agents of the county. They could not, therefore, ratify a subscription without a vote of the county, because they could not make a subscription in the first instance without such authorization. It would be absurd to say that they could, without such vote, by simple expressions of approval or in some other indirect way give validity to acts when they were directly in terms prohibited by statute from doing those acts until after such vote was had. That would be equivalent to saying that an agent, not having the power to do a particular act for his principal, could give validity to such act by its indirect recognition."[1] The court took occasion, however, to say: "We do not mean to intimate that liabilities may not be incurred by counties independent of the statute. Undoubtedly they may be. The obligation to do justice rests upon all persons, natural and artificial, and if a county obtains the money or property of others without authority, the law, independent of any statute, will compel restitution or compensation. But this is a very different thing from enforcing an obligation attempted to be created in one way when the statute declares that it shall be created in another and different way."[2]

§ 453. **Rules as to statutes legalizing a prior issue of bonds.**— Where an election authorizing aid bonds was absolutely void, because called and ordered by persons not authorized, the legislature of Illinois was held to be powerless under the State Constitution to validate bonds issued under the vote by subsequent enactment and require the issuing of the bonds peremptorily.[3] The United States Supreme Court has sustained the validity of certain statutes legalizing municipal subscriptions where the subscription to stock and issue of bonds in aid of railroads have been effected by not strictly complying with the laws in the matter of election of the voters upon the subject or otherwise, as only giving effect to the wishes of the corporate authorities.[4] A statute subsequently passed by the Illinois legislature

[1] Citing McCracken *v.* City of San Francisco, 16 Cal. 624.

[2] Marsh *v.* Fulton County, (1870) 10 Wall. 676, 683, 684.

[3] Gaddis *v.* Richland County, 92 Ill. 119.

[4] Bolles *v.* Brimfield, (1887) 120 U. S. 759; Anderson *v.* Santa Anna, 116 U. S. 356; Grenada County Supervisors *v.* Brogden, 112 U. S. 261. Municipal aid bonds held not validated by an act of the legislature ratifying them in

amended the charter of this railroad company and attempted in such amendments to validate all contracts between the company and municipalities, whereby the municipalities agreed to sell to the railroad company at a nominal price the stock for which they had subscribed. The curative effect of this statute was urged upon the United States Circuit Court of Appeals for the seventh circuit, but the court held the statute had no effect where the contract was made by the municipal authorities without being admitted to popular vote, as required by law, the legislature not having the power to impose an obligation upon a municipality without its consent legally expressed.[1]

Williams *v.* People, 132 Ill. 574; s. c., 24 N. E. Rep. 647; disapproving Jonesboro City *v.* Railroad Co., 110 U. S. 192; s. c., 4 Sup. Ct. Rep. 67. The effect of a curative act of the legislature. Atchison, Texas & Santa Fe R. R. Co. *v.* Jefferson County, 17 Kans. 29.

[1] Post *v.* Pulaski County, (1892) 49 Fed. Rep. 628. BLODGETT, D. J., said: "In reference to the validity of the statute, we cannot express our own views more clearly or forcibly than by quoting from the opinion of [Mr. Justice BAILEY] in the case [of Choisser *v.* People, 140 Ill. 21; s. c., 29 N. E. Rep. 546] in which he says: 'The only proposition which had been submitted to the vote of the people of the county, and the only proposition which, under existing laws, the County Court had power to submit to them, was that of making a subscription to the capital stock of the railroad company, the stock to be received as the consideration, and, presumably, the equivalent, for the county bonds to be issued in pursuance of the subscription. The proposition to donate ninety-five thousand dollars in county bonds to said railroad company was never submitted to the people of said county, was never voted upon by them, and could not, under the existing laws, have been submitted to such vote. The subsequent contract entered into by the County Court, to sell back the stock subscribed for, for a nominal consideration, so as to effectually terminate the proposition to subscribe one hundred thousand dollars to the capital stock of said company, to which the people of the county had given their assent, into a proposition to donate to the railroad company ninety-five thousand dollars of county bonds, to which the people of the county had not, and could not have, given their assent, was clearly void, so as to confer no rights and impose no obligations. * * * In the present case the amendatory act of 1869, if effectual at all, can be held to operate only by way of validating a contract for a donation which, by reason of want of power, as well as the absence of either an intention or opportunity on the part of the legal voters of the county to give their assent to it, was *ultra vires* and void. Declaring such void contract to be valid and binding, and providing that it should be carried into effect in good faith, as said amendatory act undertook to do, was an attempt to impose upon the county an obligation in aid of the railroad without its own consent, expressed in any legal form." Where a subsequent act legalizing the proceedings of a county in subscribing to, and paying for, stock of a railroad company was held to have cured all defects, see Hall *v.*

§ 454. **Recitals on face of aid bonds — their effect.** — A recital in county bonds, that they are issued "pursuant to an order of the County Court," puts all persons dealing in the bonds upon inquiry as to the terms of the order.[1] Where there was a recital in a municipal bond that it was issued in payment of a subscription made in pursuance of a vote of the people at an election specified in the recital, and there was no law authorizing such election and subscription, the holder of the bond was held to have notice by the recital of the illegality of the subscription.[2] Should bonds purporting to have been issued by a county contain no recitals of an election, or of proceedings and orders of the county authorities, being mere promises to pay, purchasers or holders of the bonds will be chargeable with notice of whatever appears upon the face of the county records.[3] A purchaser of county bonds issued in aid of a railroad company is not bound to go behind the records, and where such records show enough upon the matter of authority to issue the bonds to justify him in taking them, he cannot be required to go behind them and show that the record is true. He may rely upon the records for the facts stated in relation to he vote of the county authorizing the subscription to the stock. And the county cannot afterwards question the regularity of its own proceedings.[4] Under its general powers to lend its credit in

Baker, 74 Wis. 118; s. c., 42 N. W. Rep. 104.

[1] Post *v.* Pulaski County, (1892) 49 Fed. Rep. 628.

[2] Barnes *v.* Town of Lacon, 84 Ill. 461.

[3] Lewis *v.* Bourbon County, 12 Kans. 186.

[4] Clapp *v.* County of Cedar, 5 Iowa, 15; Meyer *v.* Muscatine, 1 Wall. 384; Lynde *v.* Winnebago County, 16 Wall. 6. See Livingston County *v.* First National Bank of Portsmouth, (1888) 128 U. S. 102, as to what recitals and under what statement of facts, a county would be estopped from urging as against a *bona fide* holder of the bonds of the county issued in aid of a railroad company, the existence of any mere irregularity in the making of the subscription or the issuing of the bonds. In Kimball *v.* Town of Lakeland, (1890) 41 Fed. Rep. 289, it appeared that the General Statutes of Minnesota authorized municipal corporations to issue railroad aid bonds, provided an agreement is reached between the railroad company and the municipality in either one of two modes. In 1879 this act was amended so as to allow but one mode of making such agreement. In 1880 the bonds of this town were issued in pursuance of the act, upon an agreement entered into in the mode which had been repealed. The bonds recited that they were issued under the act, and that all the conditions of the act had been complied with. The federal court held that the recital in the bonds estopped the town from denying the validity of the bonds as against a *bona*

aid of railroads, a county in Kansas issued bonds in exchange for the stock of a railroad company on condition that the company build a railroad of standard gauge through the county. In issuing the bonds all the formalities required by the law, on the part of the county, were complied with. The United States Circuit Court of Appeals for the eighth circuit held that the county could not set up the defense of *ultra vires* to the action on the bonds, because the railroad company was authorized to build only a narrow-gauge railroad. These bonds bore on their face recitals that they were issued to the railroad company in payment of a subscription for stock, made by virtue of an act of the legislature (the title and date of which were given), and acts amendatory of the same, with this further statement on each bond, "the provisions and requirements of said acts, and the conditions prescribed necessary to the subscription aforesaid, and the lawful issue of this bond, having been in all respects fully and completely complied with and performed." The defense of *ultra vires* was held not to be available in the action as against a *bona fide* purchaser for value on the faith of the recitals, and without notice that the company was authorized to construct only a narrow-gauge road, and that the bonds were issued on condition that the road should be, as it in fact was, of standard gauge.[1]

fide holder for value. Citing Fulton *v.* Town of Riverton, 42 Minn. 395; s. c., 44 N. W. Rep. 257.

[1] Board of Comrs. of Kingman County *v.* Cornell University, (1893) 57 Fed. Rep. 149. It was said in the opinion: "The general doctrine is that where a contract or undertaking which has been entered into by a corporation is simply in excess of its charter powers, and the same has been fully executed, the defense of *ultra vires* cannot be successfully pleaded in a suit to enforce negotiable securities or other obligations which have issued out of the original transaction. In such cases the state is entitled to restrain the offending corporation from exercising powers that do not belong to it, or to oust it of its franchises, in a proper proceeding brought for that purpose, but it is ordinarily held that in collateral suits between private litigants the plea of *ultra vires* is not available as a defense. Bank *v.* North, 4 Johns. Ch. 370; Bank *v.* Matthews, 98 U. S. 621; Gold Mining Co. *v.* National Bank, 96 U. S. 640; Whitney Arms Co. *v.* Barlow, 63 N. Y. 62; Bradley *v.* Ballard, 55 Ill. 417; Ditch Co. *v.* Zellerbach, 37 Cal. 543; Argenti *v.* City of San Francisco, 16 Cal. 255; Allegheny City *v.* McClurkan, 14 Pa. St. 81. * * * In the case of County of Macon *v.* Shores, 97 U. S. 272, it appeared that county aid had been granted to a railroad company in the form of a stock subscription and by an issuance of bonds, although the company had not accepted its charter and become organized as a corporation within the time limited by law for such acceptance of the charter and for organization thereunder. In a suit

§ 455. Bonds and coupons not claims which require presentation to county authorities before suit.—In a case involving county bonds issued in Alabama in aid of a railroad company, before the United States Supreme Court, the question of whether or not an action could be maintained upon bonds or coupons which had been attached to such bonds where they had not been presented to the Court of County Commissioners for allowance before the suit was brought, was fully discussed by that court. The result of the consideration by the court of the statutes of Alabama and the cases determined by the Supreme Court of that state, was a holding that the action was maintainable, and that the bonds and coupons did not constitute such claims as should be presented for action to the county authorities before suit could be brought upon them.[1]

against the county upon the bonds, it was held that a plea that the company had not become organized within the time limited by law constituted no defense as against an innocent purchaser of the securities. The same ruling was repeated in the case of County of Ralls *v.* Douglass, 105 U. S. 728, and in the latter case it was also held that it was not competent for the county to show by way of defense, as against an innocent purchaser of its bonds, that when they were executed a person was acting as presiding judge of the County Court who was not *de jure* a member of the court. It seems to be settled by these decisions that a purchaser for value of railroad aid bonds is not required to ascertain and to determine at his peril whether the railway corporation to whom they were voted and issued was at the time duly and regularly constituted * * *."

[1] County of Greene *v.* Daniel, (1880) 102 U. S. 187; County of Pickens *v.* Daniel, (1880) 102 U. S. 187. Chief Justice WAITE referred to the statutes of Alabama relating to granting aid to railroads, and to the cases of Shinbone *v.* Randolph County, 56 Ala. 183; Commissioners' Court of Limestone County *v.* Rather, 48 Ala. 433. Then he said: "The bonds and coupons in these cases were signed by the judge of probate of the county, as the presiding officer of the Commissioners' Court, and it seems to us that they are, in legal effect, themselves warrants on the treasurer, given by the judge of probate after an allowance by the court of the claim of the railroad company for the payment of the county subscription in accordance with the terms of the accepted proposal. The claim was, to all intents and purposes, audited by the court when the bonds were issued. The validity and amount of the liability were then definitely fixed, and warrants on the treasury given payable at a future day. The treasurer could pay them when due on presentation without further action of the court, if he had funds in his hands applicable to that purpose. In his hands they would be good vouchers for money disbursed from that fund. The provision that the coupons should be received in payment of taxes levied to meet them is entirely consistent with any idea of an unliquidated claim which required further auditing." Then, addressing himself to the remedy if such bonds or coupons were unpaid when due, the chief justice said:

§ 456. **Coupons — rules governing.**— A coupon attached to a bond issued by a county in payment of its subscription to the stock of a railroad corporation, under the authority given it by the legislature, will not be invalidated by the fact that the coupon is made payable in New York or elsewhere than at the treasury of the county issuing it.[1] Coupons for the payment of interest,

"In the state courts, under the rule as stated in Shinbone *v.* Randolph Co., 56 Ala. 183, and other cases, a *mandamus* would lie without reducing the coupons to judgment, to compel the Commissioners' Court to levy and collect the taxes necessary to pay what was due. The rule is different, however, in the courts of the United States, where such a writ can only be granted in aid of an existing jurisdiction. There a judgment at law on the coupons is necessary to support such a writ. The *mandamus* is in the nature of an execution to carry the judgment into effect. Bath County *v.* Amy, 13 Wall. 244; Graham *v.* Norton, 15 Wall. 427. A suit, therefore, to get judgment on the bonds or coupons is part of the necessary machinery which the courts of the United States must use in enforcing the claim, and the jurisdiction of those courts is not to be ousted simply because in the courts of the state a remedy may be afforded in another way."

[1] Johnson *v.* County of Stark, (1860) 24 Ill. 75. It was said by the court: "It was held by this court, in the case of The People ex rel. *v.* Tazewell County, 22 Ill. 147, that counties and municipal corporations, unless specially authorized by legislative enactment, have no power to make their indebtedness payable at any other place than at their treasury. That proceeding was an application for a writ of *mandamus*, to compel the board of supervisors to issue bonds and coupons, payable in the city of New York. The application was based upon a demand of such bonds and coupons; and as there had been no demand of such securities payable at the county treasury, the question now under consideration was not then before the court, and was not determined. The board of supervisors could not be in default until they had refused to issue bonds and coupons, authorized by law, upon a proper demand. No such demand was made in that case, and, therefore, the court could not compel them to proceed to issue such securities. This case presents the question, whether instruments evidencing their indebtedness payable specifically at any other place are void, or whether they may be upheld as payable at their treasury. This coupon on its face purports to be payable at the city of New York. The doctrine is well recognized that in exercising a power, all acts performed in excess of, or beyond, the power delegated, must be rejected as unwarranted; and if, after their rejection, there has been enough done to show a proper execution of the power, the act will be sustained, irrespective of the acts beyond the power delegated. But, on the contrary, if the acts performed beyond the authority conferred, are so inseparably connected with the acts properly performed, that, by their rejection, the power remains unexecuted, then the whole transaction must be rejected as void. When tested by this rule, it will be perceived that this coupon may be sustained as valid, and payable at the treasury of the county. The law authorized the county to issue it, and

executed at the same time and attached to municipal bonds and referred to therein, when detached are negotiable, and when matured, action may be brought upon the coupons against the corporation issuing them, provided it had power to issue the bonds.[1] Coupons attached to municipal bonds, payable to bearer, for a sum certain, assimilate to bank bills. They pass by delivery only, and may be offered in evidence under the common money counts appropriate to an action upon them.[2] The holder of an unindorsed coupon detached from a bond of a municipality is entitled to demand payment of the same, and, if refused, to sue for and recover the money in his own name.[3] Municipal bonds with coupons payable to bearer, being negotiable securities, and having all the qualities and incidents of negotiable paper, and the coupons negotiable like the bonds, it is not necessary that the holder of the coupon, in order to recover, should own the

requires no place of payment to be named. And where none is specified, it, by operation of law, is payable at the treasury. If this coupon had not contained the language, 'at the city of New York,' it would have been a legal instrument, strictly conforming to all the requirements of the law authorizing counties to issue evidences of indebtedness. If then this unauthorized portion of the coupon were rejected, it would be in conformity to the law, and, for the purpose of upholding it, the law will reject that portion as surplusage. This doctrine was announced by the very able district judge of United States District Court for Wisconsin in the case of Mygatt *v.* City of Green Bay, 1 Biss. 292, which was precisely similar to this case."

[1] Town of Cicero *v.* Clifford, 53 Ind. 191.

[2] Board of Supervisors of Mercer County *v.* Hubbard, (1867) 45 Ill. 139.

[3] Johnson *v.* County of Stark, (1860) 24 Ill. 75. It was contended in this case that the plaintiff had no legal title to the coupon sued on. The bond to which it was annexed was duly assigned to him, but there was no indorsement on the coupon. The court said: "It seems to be the well-settled doctrine that state, county, city and other bonds, and public securities of this character, are negotiable by delivery only, without indorsement, in the same manner as bank bills, especially when they are payable to bearer. Redf. on Rys. 595, and authorities cited. It is true that this coupon names no person as payee, nor is it specifically payable to bearer. But the promise is 'to pay sixty dollars on this coupon.' The promise is to pay the sum named in the instrument, and it can only be demanded by the person holding it, and precisely as if it was payable in terms to bearer. There is no room to doubt that the specified amount, by the terms of the agreement, is payable to, and may be demanded by, the holder after its maturity. Its legal effect is, that the money is to be paid on the coupon, and to the holder presenting it for that purpose."

bonds from which they are detached.[1] The defense cannot be made in an action upon coupons detached from municipal bonds that they are signed by only one of the county officers, where the bonds to which they were attached are properly signed and sealed by the officers of the county.[2]

§ 457. **A county suable on precinct bonds.**— The charter of this Kentucky railroad company authorized magisterial precincts of any county through which it passed to subscribe to its capital stock, and provided that the bonds of the county should be issued in payment of such a subscription in every respect as if such subscription was made by the county, but that such precincts should be alone bound to pay such bonds. Before the United States Circuit Court of Appeals for the sixth circuit it was objected that the county was not liable on the bonds, and that it was error in the action thereon to have rendered judgment against the county. The court held that the county was liable to actions on such bonds, but judgment against it was to be satisfied out of a tax levied on the precincts alone.[3]

[1] Thompson *v.* Lee County, 3 Wall. 327.

[2] Thayer *v.* Montgomery County, 3 Dill. 389. That interest is recoverable upon overdue coupons, see Genoa *v.* Woodruff, 92 U. S. 502; Walnut *v.* Wade, 103 U. S. 683; Koshkonong *v.* Burton, 104 U. S. 668; Aurora City *v.* West, 7 Wall. 82; Cromwell *v.* County of Sac, 96 U. S. 51; Hollingsworth *v.* Detroit, 3 McLean, 472; Beaver *v.* Armstrong, 44 Pa. St. 63; Mills *v.* Jefferson, 20 Wis. 50; Burroughs *v.* Richmond County, 65 N. C. 234; McLendon *v.* Anson County, 71 N. C. 38; Davis *v.* Yuba, 75 Cal. 452.

[3] Breckinridge County *v.* McCracken, (1894) 61 Fed. Rep. 191. The court said: "The districts subscribing were not corporations, and could not, without further legislation, execute and deliver bonds. Some one could be authorized to become the obligor. This duty was imposed on the county. This was authorized under the [following Kentucky decisions: City of Lexington *v.* McQuillan's Heirs, 9 Dana, 513; County Judge of Shelby County *v.* Shelby R. Co., 5 Bush, 226; Kreiger *v.* Railroad Co., 84 Ky. 66; Allison *v.* Railway Co., 10 Bush, 1. See, also, Carter Co. *v.* Sinton, 120 U. S. 518; s. c., 7 Sup. Ct. Rep. 650; Hancock *v.* Railroad Co., 145 U. S. 414; s. c., 12 Sup. Ct. Rep. 969]. * * * While the district subscribing is the debtor, yet in form the county is the obligor. Through the county the indebted district is to act, and through the same agency the indebted district is to be coerced by the assessment of the tax essential to meet its obligations. Such a district becomes, for the purposes of the subscription, a corporation *quoad hoc.* Kreiger *v.* Railroad Co., 84 Ky. 66; Hancock *v.* Railroad Co., 145 U. S. 409. It is suable only through the county which, in respect to the subscription, the issuance of the bonds, and the assessment of a special levy stands for and represents the debtor. The judgment was

§ 458. Rules as to pleading in such cases.—A simple allegation in the petition in an action on railroad aid bonds that "an election was duly held" to determine whether the subscription should be made, has been held to be sufficient.[1] And the plain-

properly rendered against the county, collectible only from tax levied on property in the indebted district. The charter, in this respect, is substantially like the provision construed in Davenport *v.* Dodge Co., 105 U. S. 237." In Blair *v.* Cuming County, 111 U. S. 363, a case of bonds issued under a vote of a precinct in aid of a public improvement, a case from the district of Nebraska, Mr. Justice BLATCHFORD, for the United States Supreme Court discussed this same question in these words: "This question was decided by this court in Davenport *v.* County of Dodge, 105 U. S. 237, in regard to precinct bonds issued under the same statute, and it was held that a suit against the county on coupons cut from special bonds issued by the county commissioners for the precinct, was a proper suit." It was also contended that the statute required that precinct bonds should be issued as special county bonds for the precinct by the county commissioners, and did not authorize the chairman of the board and its clerk to issue the bonds; that the county commissioners could not delegate their authority to sign and issue the bonds to any one else, or to one of their number; and that precinct bonds signed by one of the county commissioners as chairman, and attested by the clerk of the board, and coupons signed by some one as clerk, had no validity. To this it was said: "We see no force in these objections. The bonds bear the seal of the county, and purport to be issued by the board of county commissioners on behalf of the precinct. The bond states that the board, in testimony of the statements in the bond, has caused the bond to be signed in behalf of the precinct, by the chairman of the board, and to be attested by the clerk of the board (who appears by the petition to have been the clerk of the county), and that such clerk has affixed thereto the seal of the county. This was a sufficient compliance with the statute. The commissioners by statute constituted a 'board.' That was their official designation when meeting to perform any duties with which they were charged. See Gen. Stats. Neb. (1873) chap. 13, §§ 7, 14, pp. 233, 234. The attestation of the bonds by the signatures of the chairman and clerk of the board and the county seal, was proper. It was not necessary that all the commissioners should sign the bonds. What was done was not an issuing of the bonds by the chairman and clerk. The coupons in the form in which they were issued, annexed to the bond, were adopted as coupons by the statement in the body of the bond, and the question as to any one of them, when detached, is only one of genuineness and identity. The bonds are special bonds for the precinct, and contain a sufficient statement showing their special nature, that is, that they are special bonds for the precinct."

[1] Breckenridge County *v.* McCracken, (1894) 61 Fed. Rep. 191. It was said by the court: "This is substantially an averment that the election was held according to the requirements of the law. It was not, however, important that the pleader should aver the preliminary facts requisite to the exercise of the power granted by the legislature to subscribe for the stock and issue bonds in payment. The

tiff in such an action need not allege a reservation made in the bonds by the county as to the time of payment, where there was no such reservation in the act authorizing the subscription, or the power to restore the bonds was in no wise affected thereby.[1] In Edwards *v.* Bates County, 55 Fed. Rep. 436, it was held that an offer by the county, within the statutory period of limitation, to compromise its bonds at a specified percentage, which offer was declined by the holders of the bonds in suit, although accepted by the holders of all of its other bonds, was not a promise to pay or an acknowledgment of the debt, which would interrupt the running of the Statute of Limitations.[2]

power to hold an election, subscribe for stock, and issue the bonds is averred. If there was any defect in the steps preliminary to the exercise of that power, it is for the defendant to plead and show such irregularity. The performance or non-performance of acts requisite to the valid exercise of the power are matters of defense. This precise question arose in Lincoln Tp. *v.* Cambria Iron Co., 103 U. S. 412. The declaration in a suit upon certain bonds issued by a Michigan township, did not aver that an election was held to authorize the issuance of the bonds, as required by law, and did not aver certain other prerequisites to such issue. After considering the effect of a verdict for the plaintiff as a waiver of such objection to the pleading, the court said: 'But we do not think that there was any defect in the declaration to be cured. We think that it would have been good on demurrer. The township had authority by law to issue its bonds by way of a donation to a railroad. It did issue its bonds. They got into circulation as commercial securities and were purchased by the plaintiff. All the plaintiff had to do in case of non-payment was simply to sue on the bonds. If there was any defense to them by reason of want of performance of any of the requisites necessary to give them validity, or for any other cause, it was for the defendant to show it. A bond, especially a negotiable bond, is a *prima facie* obligation of the obligor, if he has capacity to make it, and is binding according to the terms and conditions apparent on its face, until the contrary be shown. Whether an alleged defense, when set up, is or is not good against the particular holder, is to be determined by the court in each case.' 103 U. S. 416. The case of Hopper *v.* Town of Covington, 118 U. S. 148; s. c., 6 Sup. Ct. Rep. 1025, is relied upon by the appellant. It is not in point. The defect in the declaration went to the power of the corporation. In that very case the court drew a distinction between the want of power and an irregularity in the exercise of the power. See, also, County of Clay *v.* Society for Savings, 104 U. S. 586."

[1] Breckenridge County *v.* McCracken, (1894) 61 Fed. Rep. 191.

[2] As to liability of a county on precinct bonds, see Blair *v.* Cuming County, 111 U. S. 363; Nemaha County *v.* Frank, 120 U. S. 41. Cases in which the bonds were held valid, Lewis *v.* Pima County, 15 Sup. Ct. Rep. 22; Wilmington, O. & E. C. R. R. Co. *v.* Board of Comrs. Onslow County, (N. C.) 21 S. E. Rep. 205. Where they were held to be invalid, Citizens' Sav. & Loan Assn. *v.* Perry County, 15 Sup. Ct. Rep. 547; German Savings Bank *v.* Franklin County, 128 U. S. 526.

CHAPTER XXIII.

MUNICIPAL AID BONDS—CITY.

§ 459. City aid bonds, generally.
460. Rules as to such bonds settled in United States Supreme Court.
461. Why state decisions should not control United States Supreme Court.
462. When the issue of aid bonds by a city is authorized.
463. When the right to municipal aid is lost by delay in constructing road.
464. The election as to aid and the effect of curative legislation.
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466. Aid to railroads outside the state.
467. Estoppel of a city to claim that bonds were wrongfully issued.
468. What will not affect the rights of bona fide bondholders.
469. When a purchaser of void municipal bonds cannot maintain an action for money had and received.

§ 459. **City aid bonds, generally.**— The constitutionality of the general law of Indiana authorizing the donation and issue of bonds in aid of railroad companies, has been regarded as settled by the Indiana Supreme Court.[1] And bonds regularly issued and delivered by the authority of that law, in the hands of a *bona fide* holder, for a valuable consideration, the court held must be regarded as public securities, and placed on a footing with bills of exchange.[2] The power to issue bonds as a simple donation is not included in the general power incident to municipal corporations to issue their bonds for existing indebtedness or for money borrowed for municipal purposes.[3] Without express power in its charter, a city cannot issue bonds in aid of a railroad company

[1] City of Mt. Vernon *v.* Hovey, (1876) 52 Ind. 563; citing Sankey *v.* Terre Haute & S. W. R. R. Co., 42 Ind. 402.

[2] City of Mt. Vernon *v.* Hovey, (1876) 52 Ind. 563; citing City of Aurora *v.* West, 22 Ind. 88; Nugent *v.* The Supervisors, 19 Wall. 241; Moran *v.* The Commissioners of Miami County, 2 Black, 722; Lee County *v.* Rogers, 7 Wall. 181; Mercer County *v.* Hacket, 1 Wall. 83; Rogers *v.* Burlington, 3 Wall. 654; Clark *v.* City of Janesville, 10 Wis. 136; State ex rel. Treadwell *v.* Commissioners, 12 Ohio St. 596; New Albany, etc., Plank Road Co. *v.* Smith, 23 Ind. 353; Board of Commissioners *v.* Bright, 18 Ind. 93. That a municipality may be compelled by *mandamus* to issue its bonds in aid of a railroad company, see Mayor, etc., Kokomo *v.* State, 57 Ind. 152.

[3] Bissell *v.* City of Kankakee, 64 Ill. 249.

as a gratuity, as, for instance, in order to drain swamps, or to secure the location of the workshops of the company in such city.[1] A city being expressly authorized to borrow money to pay for stock subscribed in aid of a railroad company, the power to determine time of payment, and to issue bonds and other evidences of indebtedness, would be implied.[2] Where the proposition submitted to the electors of a city was whether it should issue its bonds in aid of a railroad "to an amount not exceeding one million dollars," and the election resulted in favor of the proposition, the city council would have a discretionary power as to the amount of the bonds to be issued, not exceeding $1,000,000, and may confine the issue to $500,000.[3] Where the petition for a donation of bonds to a railroad company by a city, asks a donation of bonds in a certain amount without interest, the city cannot issue bonds bearing interest.[4] The fact that some members of the council of a city who voted in favor of a donation of its bonds upon a petition in aid of a railroad company, were also officers of the railroad company, has been held not to have disqualified them from acting, or the council from passing an ordinance making the donation.[5] The donation of bonds by a city in aid of a railroad is an absolute grant, and, after it is made, collection of a tax levied to pay interest on, or create a sinking fund to pay the principal of, such bonds can be enjoined only on grounds constituting a valid defense to payment of the bonds in the hands of present holders.[6] Under the General Statutes of Indiana a city might subscribe to stock of a railroad company without petition, and might issue and sell its bonds to borrow money to pay the subscription. A petition from freeholders is only

[1] New Orleans, M. & C. R. Co. *v.* Dunn, 51 Ala. 128. In City of Mt. Vernon *v.* Hovey, (1876) 52 Ind. 563, where the bonds donated in aid of a railroad company by the city had been issued to it after its consolidation with another railroad company, the Supreme Court held that an injunction would not lie in the action of a taxpayer for an injunction to restrain the collection of a tax assessed against him for the payment of the interest on these bonds and to create a sinking fund for the payment of the principal of the bonds, no irregularity in the petition of the freeholders or in the order of the common council making the donation being shown, and no irregularity in the consolidation of the companies being claimed.

[2] E., I. & C. R. R. Co. *v.* City of Evansville, 15 Ind. 395.

[3] Winter *v.* City Council of Montgomery, (1880) 65 Ala. 403.

[4] Mayor, etc., Kokomo *v.* State, 57 Ind. 152. As to interest on coupons of railroad aid bonds, see City of Pekin *v.* Reynolds, 31 Ill. 529.

[5] Mayor, etc., Kokomo *v.* State, 57 Ind. 152.

[6] Wilkinson *v.* City of Peru, 61 Ind. 1.

required in case of donation of city bonds in aid of railroads.[1] Petitioners for aid by way of donation of bonds by the city council of a city in Indiana have been held to have the right to withdraw their names from the petition, by signing a remonstrance, after the petition has reached the council and been referred to a committee. The withdrawal would have the same effect as if they had not signed.[2] Such petitions must accord with the provisions of the statute authorizing them, otherwise they will be invalid.[3] Donation under the act under which the bonds of this city were donated was held to mean an absolute gift or grant without any condition or consideration.[4] When a power to subscribe to stock of a railroad company has been conferred by a petition in the terms of the Indiana statute upon the common council of a city, the mode in which the power should be exercised, in a measure, would be necessarily left to the discretion and judgment of the common council.[5] Where, by its charter, an Indiana city was empowered to subscribe to stock "in any chartered company, for making roads to said city," the Supreme Court of that state held that a road through that city was a road to it within the meaning of its charter.[6] It was held in another case that a "railroad" was such a "road" within the meaning of such a provision in the charter of a city.[7] The receipt of bonds by the railroad company, as cash in payment of such a subscription, would not be beyond the power of either the city or railroad company.[8] Where the charter of an Indiana city provided that the city might, upon compliance with certain formalites, create a debt, and restrained the authorities, in general, to a certain rate of taxation, but at the same time authorized the corporation to construct wharves, docks, piers, water works, works for lighting city, etc., undertakings, the expense of which might far exceed the revenues of the city at the general rate of taxation, the Supreme Court held that the authority to create a debt in that provision of its charter empowered it to create a debt only

[1] Thompson *v.* City of Peru, 29 Ind. 305. See, also, City of Aurora *v.* West, 9 Ind. 74.

[2] Noble *v.* City of Vincennes, 42 Ind. 125.

[3] I., N. & S. Ry. Co. *v.* City of Attica, 56 Ind. 476.

[4] Wilkinson *v.* City of Peru, 61 Ind. 1.

[5] E., I. & C. R. R. Co. *v.* City of Evansville, 15 Ind. 395.

[6] City of Aurora *v.* West, 9 Ind. 74.

[7] E., I. & C. R. R. Co. *v.* City of Evansville, 15 Ind. 395.

[8] Ibid.

for these undertakings, and would not authorize an issue of bonds in aid of a railroad company.[1] A city cannot defeat a subscription in aid of a railroad company by setting up a parol condition inconsistent with the terms of contract of subscription.[2] The ordinary coupon bonds of a municipal corporation having authority to issue them payable to bearer or to the order of a person named, though under seal, are commercial or negotiable instruments on an equality with bank bills or bills of exchange, if, in other respects, they have the essential requisites of negotiable paper.[3] Bonds issued by a city in Alabama, in aid of a railroad corporation, under statutory authority, were held not to be negotiable paper, because on their face they were made payable on a contingency which might never happen, to wit, the completion of the railroad to that city, and also because they were payable to bearer only.[4] The title to these bonds, therefore, it was held could not pass by delivery, nor, as against the real owner, except by his indorsement and assignment.[5] Under an Alabama act authorizing a city to issue aid bonds which was silent as to the kind of currency in which the bonds were to be paid, the Supreme Court held that the city had power to make them payable "in gold coin of the United States of the present standand, weight and fineness."[6] A complaint of fraud in the election on the ques-

[1] City of La Fayette *v.* Cox, 5 Ind. 38. As to a limitation upon the rate of taxation by a city to pay its bonds issued in aid of a railroad company under power granted in the city's charter, see Burnes *v.* Atchison, 2 Kans. 454. As to the right of a purchaser of city bonds to presume that the necessary steps had been taken for the legal issuance of the bonds of a city in aid of a railroad company, see Atchison *v.* Butcher, 3 Kans. 104. That the collection of taxes and paying interest on bonds of a city in aid of a railroad company will not amount to a ratification of bonds issued without authority, in the absence of legislative authority to ratify, see Atchison *v.* Butcher, 3 Kans. 104. When a vote under article 11, section 14, of the Constitution of Missouri of 1865, would authorize a subscription to the stock of a railroad company, but would not validate the issue of negotiable bonds in payment of the subscription, see Hill *v.* City of Memphis, 134 U. S. 198; s. c., 10 Sup. Ct. Rep. 562. What defense is not open to a city in an action by a railroad company to recover money voted to it by the city and payable when the road is completed for use, see Manchester & Keene Railroad *v.* City of Keene, 62 N. H. 81.

[2] Evansville, etc., R. R. Co. *v.* City of Evansville, 15 Ind. 395.

[3] Blackman *v.* Lehman, 63 Ala. 547; Colt *v.* Barnes, 64 Ala. 108; State *v.* Cobb, 64 Ala. 127; Reid *v.* Bank of Mobile, 70 Ala. 199; Gilman *v.* N. O. & S. R. R. Co., 72 Ala. 566.

[4] Blackman *v.* Lehman, 63 Ala. 547.

[5] Ibid.

[6] Judson *v.* City of Bessemer, 87 Ala. 240; s. c., 6 So. Rep. 267. As to the power of cities to extend aid to railroad corporations, see Bard *v.* City

tion of taking stock or issuing bonds must be made in proper time and before any right has accrued under the election.[1] The issuing of the bonds of a municipal corporation to a railroad company being dependent upon the condition that the road of the company should be completed to a certain city within a given time, the Illinois Supreme Court held that the completion of the road to about a mile from the city and an arrangement with another company, the road of which it intersected, that it should run its trains over that other road, should be regarded as a substantial compliance with the condition.[2] Where bonds have been issued by a municipal corporation, regular on their face, negotiable in form, and have passed into the hands of third persons as purchasers for value, who are not charged with knowledge or notice of any irregularity in their issue, taxpayers cannot enjoin the collection of a municipal tax levied to pay the interest on them.[3] A city in Illinois was authorized to subscribe to the capital stock of a railway company upon an affirmative vote of the people, to be paid for in corporate bonds to run not exceeding ten years, and to bear not exceeding ten per cent interest. The proposition submitted and voted was that the bonds to be issued should be made payable in not less than twenty years and bear interest at the rate of eight per cent per annum. This proposition was held to be materially variant from the one authorized by law in respect to the time the bonds had to run before due, and the submission was held to be in excess of the power conferred, and the vote upon it without any binding authority; it

of Augusta, 30 Fed. Rep. 906; Bartemeyer *v.* Rohlfs, (Iowa) 32 N. W. Rep. 673; Perrin *v.* City of New London, (Wis.) 30 N. W. Rep. 623. City bonds in payment of a subscription to stock of a railroad company held unauthorized in Katzenberger *v.* City of Aberdeen, 7 Sup. Ct. Rep. 947. As to the effect of noncompliance on the part of a railroad corporation with the conditions connected with its use of part of the public domain of a city under a grant of the same by statute, and the assent of the city authorities, see City of Macon *v.* East Tennessee, Virginia & Georgia Ry. Co., 82 Ga. 501; s. c., 9 S. E. Rep. 1127.

[1] Robertson *v.* City of Rockford, 21 Ill. 451; Johnson *v.* Stark County, 24 Ill. 75; Perkins *v.* Lewis, 24 Ill. 208; Butler *v.* Dunham, 27 Ill. 474.

[2] People *v.* Holden, 82 Ill. 93.

[3] State ex rel. Stow *v.* City Council of Montgomery, (1883) 74 Ala. 226. In Hunt *v.* Fawcett et al., County Commissioners, (Wash. 1894) 36 Pac. Rep. 318, the Supreme Court held, in a taxpayer's action against the commissioners, that he was entitled to an injunction to restrain them from issuing certain bonds, as the debt proposed to

was also held that the issue of the bonds voted could not be compelled by the courts.[1] A municipal corporation that has lawfully contracted a debt for legitimate purposes has been held, by a majority of the Pennsylvania Supreme Court, to have power, unless restricted by its charter, or prohibited by statute, to issue its bonds in payment of the debt; further, that such power was not restricted by a special statute authorizing the corporation to borrow money from time to time, for city purposes, as might be required, not exceeding a certain amount, and issue bonds therefor.[2] There is included in the power to subscribe to the stock of a railroad company a power to contract a debt for that purpose; a city may, therefore, issue its bonds for such a subscription.[3] A

be incurred was beyond the limitation of indebtedness allowed the corporation to incur and had not been properly ratified or validated, and further the arrangement with a trust company for the sale of the bonds by which the latter was to be allowed commissions, etc., of a large amount, violated the requirement of law that they should not sell them below par.

[1] Cairo & St. Louis R. R. Co. *v.* City of Sparta, 77 Ill. 505. Where a statute of Tennessee was held not to authorize an election for bonds in aid of a railroad corporation, or the issue of the bonds by the city, and the bonds were held not enforceable by the holders. Norton *v.* Taxing District of Brownsville, 129 U. S. 479; s. c., 9 Sup. Ct. Rep. 322. Where it was held that a judgment by the holder upon some of the bonds did not estop the city from claiming that the statute authorizing them had been abrogated by the constitutional amendment of 1870. Taxing District of Brownsville *v.* League, 129 U. S. 493; s. c., 9 Sup. Ct. Rep. 327, holding that the bondholder was not entitled to a *mandamus* to compel a levy of taxes to pay his judgments. Bonds of a city in Illinois held to be invalid by reason of non-completion of the road of the railroad company, in aid of which they were voted and issued, in time, in Eddy *v.* People, 127 Ill. 428; s. c., 20 N. E. Rep. 83. Where municipal bonds in aid of a railroad have been held void under the Constitution of Illinois of 1870. Casey *v.* People, (Ill.) 24 N. E. Rep. 570. Where a statute of Missouri providing for the funding of debts of incorporated towns and empowering them to issue their bonds in payment of such indebtedness, but providing for no vote as a prerequisite to their issue, was held in contravention of the Constitution of the state of 1865, article 11, section 14. Hill *v.* City of Memphis, 134 U. S. 198; s. c., 10 Sup. Ct. Rep. 562.

[2] City *v.* Commonwealth, 84 Pa. St. 487; s. c., 4 W. N. C. (Pa.) 385.

[3] Commonwealth *v.* Pittsburgh, 41 Pa. St. 278; Commonwealth *v.* Comrs. of Allegheny, 43 Pa. St. 400. As to power in municipal corporations to borrow money, implying power to issue its bonds therefor, see Bunch's Exr. *v.* Fluvanna County, (1890) 86 Va. 452; Rogers *v.* Burlington, 3 Wall. 654; Seybert *v.* Pittsburg, 1 Wall. 272; Middleton *v.* Allegheny County, 37 Pa. St. 241. See, as to the power of the legislature of Iowa to authorize a city to subscribe for and take stock in a railway company, to issue its bonds therefor, and to lay a

municipal subscription to the stock of a railroad company would not be invalidated by a change of termini of the road in the power of the railroad company to make.[1] Should a subscription in aid of a railroad company be authorized, on conditions subsequent, the issuing of bonds in payment of the subscription by the municipality would be evidence either of performance of the conditions by the railroad company or a waiver of the conditions by the municipality.[2] Where a municipality has provided funds to meet the interest on its bonds at maturity, it will not be liable for interest on the bonds, after maturity.[3] City officers have been held to have been properly enjoined from selling bonds of the city below par, under the guise of allowing commissions upon the sales, in Pennsylvania.[4]

§ 460. Rules as to such bonds settled in United States Supreme Court.—"The following propositions," Mr. Justice Hunt of the Supreme Court of the United States, in an opinion rendered by him, has said, "may be considered as settled in this court: (1) If an election or other fact is required to authorize the issue of the bonds of a municipal corporation, and if the result of that election or the existence of that fact is by law to be ascertained and declared by any judge, officer or tribunal, and that judge, officer or tribunal, on behalf of the

tax to pay the interest thereon, as also its power to give validity to bonds as formally issued for such purposes, Rogers *v.* Keokuk, 154 U. S. 546, following Gelpcke *v.* Dubuque, 1 Wall. 175. See Rogers *v.* Lee County, 154 U. S. 547. See a note, 1 Atl. Rep. 109, as to power to issue municipal bonds and the rights of *bona fide* holders.

[1] Commonwealth *v.* Pittsburgh, 41 Pa. St. 278.

[2] Commonwealth *v.* Pittsburgh, 43 Pa. St. 391. That the holders of old bonds of a municipal corporation cannot be compelled to receive the new bonds authorized by a statute to be issued for the redemption of the old ones, at a premium which the new bonds may command in the market, see Lloyd *v.* City, 134 Pa. St. 545.

[3] Friend *v.* City, 131 Pa. St. 305. That interest is recoverable on coupons after payment of the coupons is unjustly rejected and refused, see Mills *v.* Jefferson, 20 Wis. 50; Aurora City *v.* West, 7 Wall. 82; North Penn. Railroad *v.* Adams, 54 Pa. St. 94; San Antonio *v.* Lane, 32 Tex. 405; Brainerd *v.* New York & Harlem R. R. Co., 25 N. Y. 496; Connecticut Mut. Life Ins. Co. *v.* Cleveland, etc., R. R. Co., 41 Barb. 9; New Albany Plank Road Co. *v.* Smith, 23 Ind. 353; Morris Canal & Bkg. Co. *v.* Lewis, 12 N. J. Eq. 323. As to the power of municipalities to contract to pay interest on their bonds, free from taxes, see Trust Co. *v.* City, 102 Pa. St. 387.

[4] Whelen's Appeal, 108 Pa. St. 162.

corporation, executes or issues the bonds, with a recital that the election has been held, or that the fact exists, or has taken place, this will be sufficient evidence of the fact to all *bona fide* holders of the bonds. (2) If there be lawful authority for the municipality to issue its bonds, the omission of formalities and ceremonies, or the existence of fraud on the part of the agents of the municipality issuing the bonds, cannot be urged against a *bona fide* holder seeking to enforce them.[1] (3) There must, however, be an original authority by statute to the municipality to issue the bonds. Municipal corporations have not the power, except through the special authority of the legislature, to issue corporate bonds which will bind their towns; neither have they the power to sell or mortgage the lands belonging to such towns without special authority.[2]

§ 461. **Why state decisions should not control United States Supreme Court.**— There was testimony on the trial of this case tending to prove that a registration had been made of the qualified voters of the county, and that it showed over 1,000 such voters. The vote cast at the election, upon the question of subscription of bonds in aid of the railroad company, was for the subscription, 510, and against, 98; that is, more than two-thirds of those who actually voted assented to the subscription, but not two-thirds of the qualified voters as shown by the registration. Several decisions of the Supreme Court of Missouri, the state in which was the county making the subscription and issuing the bonds, were cited to the Supreme Court of the United States, the latest being that of State *v.* Harris, 96 Mo. 29, in which that court had held that two-thirds of those actually voting was not sufficient, and that it must appear that two-thirds of the qualified voters, as ascertained by the registration, assented to the subscription, and it was said that the Supreme Court of the United States should follow the settled construction placed upon its statutes by the Supreme Court of the state. To this Mr. Justice Brewer, for the United States Supreme Court, said: "This question has been thoroughly discussed in this court, and it is

[1] Citing Grand Chute *v.* Winegar, 15 Wall. 355; Commissioners of Knox County *v.* Aspinwall, 21 How. 539; Gelpcke *v.* Dubuque, 1 Wall. 203; Moran *v.* Miami County, 2 Black, 722.

[2] Kenicott *v.* Supervisors, (1872) 16 Wall. 452, 464, 465; citing, on last proposition, Marsh *v.* Fulton County, 10 Wall. 676.

unnecessary to enter into a re-examination of it. These decisions [from Missouri] were made after the issue of the bonds, and cannot be deemed controlling."[1] The Supreme Court of the United States, in a case before it involving the validity of an act of the legislature of Wisconsin, were urged that the court was bound by a decision of the state Supreme Court that this act was unconstitutional, reported as Whiting *v.* Fond du Lac Company, 25 Wis. 188. The court declared these general principles that it would follow, as of obligation, the decisions of the state courts only on local questions peculiar to themselves, or on questions respecting the construction of their own Constitution and laws; that whether or not the construction and maintenance of a railroad owned by a corporation, and constructed and maintained under a statute of a state authorizing such construction and maintenance, is a matter in which the public has any interest of such a nature as to warrant taxation by a municipal division of the state in aid of it, is not such a question. It is one of general law. If a contract when made was valid under the Constitution and laws of a state, as they had been previously expounded by its judicial tribunals, and as they were understood at the time, no subsequent action by the legislature or the judiciary will be regarded by this court as establishing its invalidity. A railroad is a public highway. Being so, and thus a road of public use, a state may impose a tax in furtherance of that use, even though the road itself be built and owned by a private corporation. These principles they then applied to the case at bar, and held the act of the legislature of Wisconsin, authorizing a vote of the people of this particular county upon the question whether they would aid the building of a certain railroad, and if they voted in favor of aiding, authorizing the issue of county orders for money to aid in the building, to have been a proper exercise of legislative authority, and the county charged on orders issued by it and given to the road by way of donation.[2]

[1] Knox County *v.* Ninth National Bank, (1893) 147 U. S. 91, 99; citing Cass County *v.* Johnston, 95 U. S. 360; Daviess County *v.* Huidekoper, 98 U. S 98; Douglass *v.* Pike County, 101 U. S. 677; Carroll County *v.* Smith, 111 U. S. 556.

[2] Olcott *v.* Supervisors, (1872) 16 Wall. 678. The cases cited and most of them reviewed were: Havemeyer *v.* Iowa City, 3 Wall. 294; Gelpcke *v.* City of Dubuque, 1 Wall. 175; Ohio Life & Trust Company *v.* Debolt, 16 How. 432; Pratt *v.* Brown, 3 Wis. 612; Robbins *v.* Railroad Company, 6 Wis. 641; Hasbrouck *v.* Milwaukee, 13 Wis. 37; Soens *v.* Racine, 10 Wis. 280; Brodhead *v.* Milwaukee, 19 Wis.

§ 462. **When the issue of aid bonds by a city is authorized.** —The city council of an Illinois city, in conformity with a vote of the people at an election which had been authorized by a resolution of that body previously, passed an ordinance empowering and directing the mayor to subscribe a specified amount, payable in city bonds, to the capital stock of a railroad company, a Missouri corporation, which was to run its road into the Illinois city, the issue and payment of the bonds conditioned upon a certain expenditure in a certain way by the corporation, with a guaranty that the proceeds of the bonds should be expended in that manner. The next day the subscription was made by the mayor. Afterwards, the general assembly of Illinois, by act, legalized and confirmed the action of the city council in ordering the vote and in all respects whatever relating to this transaction. A part of the bonds were delivered at one time and the balance later after a change of the Constitution of the state, negotiable in form and payable to the order of the railroad company or bearer, at a certain bank in New York city, they purporting to have been issued under and by virtue of the ordinance first passed and of the act of the legislature legalizing and confirming the action of the council. In an action upon coupons taken from some of the bonds first delivered, to recover the amount due upon the coupons, the findings of the court were that all the bonds from which the coupons were detached had been purchased for value before maturity, in open market in the usual course of business and without notice of any infirmity therein; that the conditions on the part of the railroad company had been complied with, and that the city, for six years after issuing the bonds, had paid the interest upon the bonds, and by its agent in meetings of the corporation had voted upon its stock. In the action the validity of the bonds was brought in question. The Supreme Court of the United States held that the authority of the city to issue these bonds was not determinable by the provisions of the Constitution of 1870, which — saving municipal subscriptions made under existing laws by a popular vote prior to its adoption — declared

652; Clark *v.* Janesville, 10 Wis. 136; Bushnell *v.* Beloit, 10 Wis. 195; Beekman *v.* Saratoga & Schenectady R. R. Co., 3 Paige, 45; Bloodgood *v.* Mohawk & Hudson R. R. Co., 18 Wend. 1; Worcester *v.* Railroad Company, 4 Met. 564; Charles River Bridge *v.* Warren Bridge, 7 Pick. 495; Gibbons *v.* Mobile & Great Northern R. R. Co., 36 Ala. 410.

that "No county, city, town, township or other municipality shall ever become subscriber to the capital stock of any railroad or private corporation or make donation to or loan its credit in aid of such corporation: *Provided, however*, that the adoption of this article shall not be construed as affecting the rights of any such municipality to make such subscriptions when the same have been authorized, under existing laws, by a vote of the people of such municipalities prior to such adoption." "This is quite clear," it is said in the opinion rendered, "in view of section 24 of the schedule of that Constitution, which provides: 'Nothing contained in this Constitution shall be so construed as to deprive the general assembly of the power to authorize the city of Quincy to create any indebtedness for railroad or municipal purposes, for which the people of said city shall have voted, and to which they shall have given by such vote their assent prior to [a certain date]'" with some provisions.[1]

[1] Quincy *v.* Cooke, (1882) 107 U. S. 549. Mr. Justice HARLAN, in the opinion, then referred to an Illinois decision as follows: "The Supreme Court of Illinois, in Q., M. & P. R. R. Co. *v.* Morris, 84 Ill. 410, had occasion to consider the scope and effect of that section. In that case an election was held August 7, 1869, under the authority of a resolution of the city council, to take the sense of the people upon a subscription to the capital stock of the Quincy, Missouri and Pacific Railroad Company, also a Missouri corporation, whose road lay wholly within that state. That election was held without any law authorizing a vote on the question, or empowering the city to become a stockholder in that company. But, by an act passed July 1, 1871, after the Constitution of 1870 went into operation, the city of Quincy, subject to the terms and requirements embodied in the proposition submitted to the people, was authorized to make, upon such conditions as the city council deemed best, a subscription to the stock of that company, for which the people may have voted prior to the thirteenth day of December, 1869. The act further provided: 'Any election held in said city prior to said day, for the purpose of such vote being taken, and any contract or subscription made, or to be made, by said city to the capital stock of said railroad company in pursuance thereof, and any bonds or other evidences of such indebtedness issued or to be issued by said city are hereby declared valid.' Under that act the subscription was made and bonds issued, and the controlling question was as to their validity. The court, waiving any expression of opinion as to the validity of that part of the act which in terms purported to legalize the election, decided: That the obvious effect and intent of the twenty-fourth section of the schedule of the Constitution were to leave the action of the city of Quincy in assuming by vote prior to December 13, 1869, to create indebtedness for a railroad subscription and the power of the legislature over it, 'unaffected by the Constitution of 1870; in other words, to leave the vote and the power of the legislature to confer the right to take stock precisely as they would have been under the Constitution of 1848;'

§ 463. **When the right to municipal aid is lost by delay in constructing road.**— A special law empowering a municipal corporation of Minnesota to issue its bonds in aid of the construction of a railroad provided for a popular vote upon the proposition to issue bonds; that the proposal to be voted on should designate *the period within which the road must be built in order to entitle it to the benefit of the bonds;* that the bonds when voted should be delivered "in escrow" to designated persons as commissioners, to be by them delivered to the railroad company upon full and complete compliance with the terms of the act; and that if the company should fail to comply with such conditions it should be the duty of such commissioners to *forthwith* return the bonds to the city council. Such a proposal, fixing the first of November as the time within which a railroad should be completed into the city ready for operation, was submitted to the people, and the vote was in favor of issuing the bonds. The road was to be built partly across the right of way of another company, and the latter had it enjoined from crossing. From this came delay, and the road of the company which was to be aided by the bonds was not completed and in full operation until the fifteenth of November. Certain taxpayers of the city brought an action to restrain the commissioners holding the bonds from delivering them to the railroad company, and they were by judgment of the court perpetually enjoined. The case was appealed to the Supreme Court of the state, and that court held that the completion of the road by the time specified was a condition precedent, and that by reason of the failure of the company to comply therewith it was not entitled to the bonds.[1]

that the city council were the corporate authorities of Quincy, upon whom, within the meaning of the Constitution of 1848, the legislature could confer, without the intervention of a popular vote, authority to make the subscription and issue the bonds; that section 24 of that schedule embraced a vote taken without authority of law prior to December 13, 1869, because, had the vote been legal, the language 'for which the people of said city shall have voted, and to which they shall have given, by such vote, their assent,' would have been unnecessary in view of the proviso in the general section forbidding municipal subscriptions in aid of railroad corporations; lastly, that the construction of the Quincy, Missouri and Pacific railroad, although no part of it lay in Illinois, was a corporate purpose of the city of Quincy, because thereby its trade and commerce were increased, its property enhanced in value and its welfare promoted."

[1] McManus *v.* Duluth, Crookston & Northern R. Co., (1892) 51 Minn. 30; s. c., 52 N. W. Rep. 980. *Arguendo,* the court said: "While the provisions

§ 464. The election as to aid and the effect of curative legislation.— The power of the city to issue the bonds involved in this case was denied upon these principal grounds: 1. That the election held under the sanction of the city council, and the action of that body in directing the subscription to be made were of no legal effect, since the election was held without authority of law, and other subscriptions were made when there was no legislative authority to create such indebtedness. 2. That with-

of the special act constituted a part of the proposal of the railroad company, and of the petition upon which the vote was taken, it was more than a mere term or element in a contract. It was a *law* controlling the action of the city. The municipality had only such power as was conferred by this act to issue bonds in aid of this undertaking. Whatever conditions the law imposed, relating to the exercise of this power, must be complied with. The power conferred by the legislature is not to be extended, nor the express conditions restricted, by doubtful construction. Dill. Mun. Corp. 90, 91." The court, construing the act, further said: "The period for construction, under the act referred to, cannot be regarded as unessential and as not intended to be strictly complied with without disregarding language, the plain, natural import of which is to the contrary, or at least without a free, liberal construction in favor of those claiming under the power, contrary to the rule of construction in such cases. In the significant language which we have recited there is little room for construction or for doubt as to the meaning. '*The period within which said road must be built, * * * in order to entitle said railroad to the benefit of the bonds,*' was required to be and was stated in the petition or proposal upon which the people voted. It was required to be, and was, one of the conditions of the contract thus entered into. The ordinary, natural import of the language is that '*in order to entitle said railroad company*' to the bonds voted it '*must*' construct the road within the period of time stated. Further provisions of the law, above recited, make even more clear the correctness of this construction. As has just been said, this provision as to the time for construction was certainly one of the conditions or terms upon which the bonds were to be, and were voted. It is one of the 'conditions' afterwards referred to in the act, where it is said that if the company shall 'fail to comply with such conditions' it shall be the duty of the commissioners to '*forthwith*' return the bonds to the city council, which is as much as to say that they are not to be delivered to the railroad company. It may be added that the proposal of the railroad company, which was incorporated in the petition for the election, and upon which the bonds were voted, was 'to build and complete ready for operation, by or before November 1, 1889.' In support of the conclusion that the provision in the law and in the contract, as to the time within which the road should be constructed, was in the nature of a condition precedent, and that by reason of its failure to comply with that requirement the railroad is not entitled to the bonds, may be cited Bohn Mfg. Co. *v.* Lewis, 45 Minn. 164; s. c., 47 N. W. Rep. 652; Winona *v.* Minnesota Ry. Const. Co., 27 Minn. 415; s. c., 6 N.

out such authority no subscription could be legally made. 3. That the curative act of March 27, 1869 [legalizing the bonds, etc.], was invalid, because it assumed to impose indebtedness upon the city without the consent of its corporate authorities. The Supreme Court of the United States held that the corporate authorities of the city, after the passage of the act legalizing the bonds, had authority to issue them.[1]

W. Rep. 795, and 8 N. W. Rep. 148; Hodgman *v.* Chicago & St. P. Ry. Co., 20 Minn. 48; Memphis, K. & C. Ry. Co. *v.* Thompson, 24 Kans. 170; Falconer *v.* Buffalo & J. R. Co., 69 N. Y. 491; Portland & O. C. R. Co. *v.* Inhabitants, etc., of Hartford, 58 Me. 23; Eddy *v.* People, 127 Ill. 428; s. c., 20 N. E. Rep. 83."

[1] Quincy *v.* Cooke, 107 U. S. 549. It was said by the court: "In support of the position taken by the city, counsel refer to numerous decisions of the Supreme Court of Illinois, construing the [section] of the Constitution of 1848 which provides that 'the corporate authorities of counties, townships, school districts, cities, towns and villages may be vested with power to assess and collect taxes for corporate purposes.' From those decisions the following propositions, among others, may be deduced: That the clause was intended to define as well the class of municipal officers upon whom the power of taxation, for local purposes, might be conferred, as the purposes for which such power could be constitutionally exercised; that by the phrase 'corporate authorities' must be understood those municipal officers who were selected with some reference to the creation of municipal indebtedness, and who were either directly elected by the population to be taxed, or appointed in some mode to which they have given their assent; that the construction of a railroad, at least one within or near a county, township, town, village or city, was a corporate purpose of such municipality, and that a debt for a subscription to the stock of a railroad corporation, or for bonds in payment thereof, could not be imposed upon a municipal corporation without the consent or against the will of its corporate authorities. But it has been quite as distinctly ruled by the Supreme Court of Illinois that the city council, and not the voters of an incorporated city, were its corporate authorities within the meaning of the Constitution of 1848, and if empowered by legislative enactment could, under that instrument, subscribe to the stock of a railroad corporation, and issue bonds in payment thereof, without submitting the matter to popular vote. Such was the decision in Q., M. & P. R. R. Co. *v.* Morris, 84 Ill. 410, where the court reaffirmed the ruling upon this point in Keithsburg *v.* Frick, 34 Ill. 405, 421. In the latter case a subscription made by a town to the capital stock of a railroad corporation — without authority of law, as was alleged — was, by an act passed after the town was incorporated under a special charter, declared to be legal, and bonds authorized to be issued therefor. The court said: 'It is by no means a necessary element in these subscriptions that there should be a vote of the inhabitants of the town or city authorizing them. It is competent for the legislature to bestow the power directly on the corporation without any intermediary, as they did in this case.' In

§ 465. **This case distinguished from others.**— The court distinguished this case as follows: "This case is clearly distinguishable from those in which the legislature has attempted to impose upon a municipal corporation, without the consent of its corporate authorities, an indebtedness for subscription to the corporate stock of a railroad corporation. The cases mainly relied on by counsel for the city are those in which certain officers of limited authority were, in terms or in effect, required by legislative enactment to issue bonds or incur indebtedness in the name of a municipality, without the consent, expressed in legal form, of those who were, in the constitutional sense, its corporate authorities. Here there can be no question but that the city council are the corporate authorities of Quincy. And there is no ground whatever upon which to rest the suggestion that the indebtedness was created without their consent. In no just sense were they compelled to issue bonds in exchange for stock in the railroad company. If, as claimed by the city, the act of March 27, 1869, was inoperative in so far as it assumed to legalize and confirm what had been previously done without the sanction of law, nevertheless by that act it was intended to confer upon the city council power, in execution of the expressed will of the

Marshall *v.* Silliman, 61 Ill. 218, 225, the right of the legislature to grant such an authority to the trustees of an incorporated town was conceded. And in Williams *v.* Town of Roberts, 88 Ill. 11, 21, the court, speaking by SCHOLFIELD, Ch. J., said: 'County boards, such as boards of supervisors, county commissioners, etc., and the municipal authorities of incorporated cities, towns and villages, may, when empowered so to do by proper legislation, subscribe for the stock of railroad corporations without first submitting the question to the electors of the municipality. They are elected as representatives of the electors, and theoretically, in appropriate cases, their acts are the acts of those they represent. Hence it has been held where a vote of the electors has been required as a precedent condition to the making of a subscription for stock in a railroad company, and the law prescribing the mode of calling and holding the election has not been observed, inasmuch as the legislature might have empowered the municipal authorities to make the subscription without first submitting the question to the electors, it may, by a subsequent enactment, declare the non-compliance with the law in the holding of the election of no consequence, and validate the subscription, in other words, validate the subscription without reference to the election. This, however, it will be observed, is upon the theory that power to make the subscription does not in any degree necessarily depend upon a vote of the electors of the municipality upon that question, but solely upon the will of the legislature.' The authorities to which we have referred sustain the judgment against the city."

voters, to issue bonds to the amount of $100,000 for stock in this railroad company. The vote of the electors, we have seen, was not essential to the validity of bonds issued, under legislative sanction, by the corporate authorities of the city. The city council was not required and directed, but only empowered, to proceed as if they had been originally invested with authority to make the subscription. The legislature, in substance, declared, as it might constitutionally have done, that the corporate authorities of the city had its consent to issue bonds to be exchanged for stock in the railroad company. If the corporate authorities could have been compelled by legal proceedings to issue the bonds, that is only another form of saying that the curative act was constitutional, and, consequently, that the bonds are valid. If, however, they could not have been so compelled, then the execution and delivery of the bonds, under the authority of the act of March 27, 1869, was a voluntary creation of indebtedness for a corporate purpose by the corporate authorities of the city."[1]

§ 466. **Aid to railroad outside the state.**— The question was raised in an Illinois case whether a subscription by a city of that state to the stock of a railroad lying wholly in the state of Missouri, was authorized as being for a corporate purpose. The Supreme Court held that the debt was legally created for a corporate purpose.[2]

§ 467. **Estoppel of a city to claim that bonds were improperly issued.**—Bonds of a city of Mississippi, which had been donated to a consolidated railroad company by authority of an act of the legislature of that state, the preliminary vote as

[1] Quincy *v.* Cooke, (1882) 107 U. S. 549, 555, 556.

[2] Quincy, Missouri & Pacific R. R. Co. *v.* Morris, (1877) 84 Ill. 411. That cities or counties of one state may aid in the construction of a railroad that lies in another state, see Railroad Company *v.* County of Otoe, 16 Wall. 667; Walker *v.* Cincinnati, 21 Ohio St. 14; McCallie *v.* Mayor, etc., 3 Head, 317; St. Joseph & Denver R. R. Co. *v.* Buchanan County, 39 Mo. 485; Bell *v.* Railroad Co., 4 Wall. 598; Copes *v.* Charleston, 10 Rich. (S. C.) 491; Stein *v.* Mobile, 24 Ala. 591. The same principle recognized in Sharpless *v.* Mayor, etc., 21 Pa. St. 147; Gelpcke *v.* Dubuque, 1 Wall. 175; Goddin *v.* Crump, 8 Leigh, 120. That subscriptions to stock of railroads on the part of cities or other municipal corporations, may be authorized by the legislature, and that such subscriptions are for a "corporate purpose," as construed in Illinois, see Prettyman *v.* Tazewell County, 19 Ill. 406; Johnson *v.* Stark County, 24 Ill. 88; Taylor *v.* Thompson, 42 Ill. 9; Chicago, Danville & Vincennes R. R. Co. *v.* Smith, 62 Ill. 268.

required by statute and other conditions having been complied with as determined by the city authorities for another company, which became a part of the consolidated company, a federal court held were legally issued to the latter. The city authorities, in an action upon overdue coupons upon some of the bonds, were held to be estopped, as against an innocent purchaser, having issued and delivered the bonds with proper recitals, from alleging that they acted wrongfully.[1] Neither could they set up as a defense that the consolidated company was authorized to build a different road from the one originally chartered, and to leave such city off its line entirely.[2]

§ 468. **What will not affect the rights of bona fide bondholders.**—In one of the most recent cases before the Supreme Court of the United States, involving the right of *bona fide* holders of the bonds of a municipal corporation, a city, which bonds were issued in payment of a subscription to stock of a railroad company in accordance with the laws of Illinois prior to the adoption of the Constitution of 1870, the restrictions of this Constitution as to donations of municipal corporations was invoked to prevent a recovery upon the coupons attached to some of those bonds upon which an action was brought by such a holder. It appeared that the bonds, in accordance with regular proceedings of the city council, were executed and delivered after certain agreements had been entered into between the city and the railroad company, in exchange for the same amount of its shares of stock which had been subscribed for by the city, and that afterwards the city had sold this stock to the company, the company returning as a consideration for the same $5,000 of the bonds of the city. This, it was contended, made, as a resultant fact, the transaction a donation of $95,000 of the bonds to the company, such a donation as was prohibited by the State Constitution of 1870. The court held that if the disposition of the stock made

[1] Denison *v.* Mayor, etc., of City of Columbus, (1894) 62 Fed. Rep. 775; citing Block *v.* Commissioners, 99 U. S. 686; Commissioners *v.* January, 94 U. S. 202; Commissioners *v.* Clark, 94 U. S. 278; Brooklyn *v.* Insurance Co., 99 U. S. 362; Moran *v.* Commissioners, 2 Black, 722.

[2] Denison *v.* Mayor, etc., of City of Columbus, (1894) 62 Fed. Rep. 775. The court said: "The rule is that, if bonds are voted to a railroad company which at that time is authorized to consolidate with other railroads, then the bonds may properly be delivered to the consolidated company." Citing Livingston County *v.* First Nat. Bank, 128 U. S. 102; s. c., 9 Sup. Ct. Rep. 18, as announcing the doctrine and reviewing the authorities.

by the city authorities was even wrong the validity of the bonds was not affected thereby; neither could such wrong, if it was a wrong, be presented as a defense against one who had purchased in good faith the bonds thus issued.[1]

§ 469. When a purchaser of void municipal bond cannot maintain an action for money had and received.— The bonds

[1] Cairo *v.* Zane, (1893) 149 U. S. 122. Mr. Justice BREWER, speaking for the court, said: "In the case of Anderson County Commissioners *v.* Beal, 113 U. S. 227, it appeared that after the bonds had been voted by the county, at an election held on September 13, 1869, the county board, on November 5, passed an order directing a subscription in accordance with the terms of the vote, and also 'that the stock above subscribed for by this board in behalf of Anderson county is hereby sold and transferred for and in consideration of the sum of one dollar, the receipt whereof is hereby acknowledged, to James F. Joy, president of said railroad company, and the chairman of this board is authorized to sign a transfer of said stock to said James F. Joy, and to assign the certificate for said stock issued to Anderson county by said railroad company, and to authorize in such assignment the necessary transfer of said stock on the books of said company.' And it was averred that the transfer thus ordered was for the benefit of the railroad company. In reference to this, Mr. Justice BLATCHFORD, speaking for the court, observed (p. 240): 'When the bonds were delivered to the company the transaction was complete, and the bonds, as they afterwards passed to *bona fide* holders, passed free from any impairment by reason of any dealing by the board with the stock subscribed for to which the county became entitled by the issuing and delivering of the bonds. The board may have committed an improper act in parting with the stock, but that is no concern of a *bona fide* holder of the bonds or coupons.' And in Maxcy *v.* Williamson County, 72 Ill. 207, it appeared, as here, that after an election authorizing a subscription of one hundred thousand dollars to the stock of a railroad company, the County Court entered into an agreement to sell the one hundred thousand dollars of stock to the railroad company for five thousand dollars, a transaction, it will be perceived, precisely like the one before us. The validity of the bonds thus issued in payment of this subscription was thereafter challenged in a suit by taxpayers to restrain the collection of taxes levied to pay the interest thereon. Their validity was sustained, and in respect to this transfer of the stock the court, on page 212, says: 'We fail to perceive how the sale of the certificate of stock to the company for five thousand dollars can in any manner affect the rights of the holders of the bonds of the county. It surely is not intended to be insisted that because the county has, by any means, lost the consideration it received for the bonds innocent holders who had nothing whatever to do with the sale of the certificate must lose their bonds.' It is said that a different rule has since been established in Illinois, and the cases of Choisser *v.* The People, 140 Ill. 21, and of Post *v.* Pulaski County, decided by the Circuit Court of Appeals for the seventh circuit (9 U. S. App. 1), are cited. But even if this were so, it was not established until long after the plaintiff had purchased these bonds, and he would doubtless be entitled to claim the benefit of the rule existing when

of the city sued here being void because issued under an act which violated the constitutional provision in Missouri declaring that the general assembly shall not authorize any city to loan its credit to any corporation unless two-thirds of the qualified voters assent thereto, it was held by the federal court that the purchaser

he made his purchase; and the facts as they appear in these two cases are substantially unlike those in the case before us. Thus, in Choisser *v.* The People, the vote to subscribe one hundred thousand dollars of stock was on October 5, 1867, and on November 28, following, an agreement was entered into between the company and the County Court, acting on behalf of the county, that one hundred thousand dollars in stock should be issued, but that the stock should be returned back to the company for the sum of five thousand dollars, payable on the redelivery to the city of that amount of county bonds. When the bonds came to be issued the record made by the County Court recited that the one hundred thousand dollars of the capital stock should be sold back to the county for five thousand dollars of county bonds, 'thereby making a payment of ninety-five thousand dollars of Saline county bonds to said company as a donation.' And no stock was in fact issued by the company, or received by the county, or delivered to the company. In short, the parties to the transaction treated it as though it was a donation of ninety-five thousand dollars of bonds, and it was this transaction which was condemned as unauthorized by a vote prior to the Constitution. Yet, even in that case, the court was careful to limit its decision to a case in which only the rights of the railroad company, the party receiving the ninety-five thousand dollars of bonds, were concerned, for it says: 'The only presumption arising from these facts is that said bonds are still in the hands of the railroad company, and no question, therefore, is presented as to how far the alleged invalidity of said bonds would be affected by those conclusive presumptions which the law raises for the protection of *bona fide* holders of commercial paper, * * * nothing is before us except the mere question of the legality of these bonds as between the county and the railroad company, the original parties thereto.' And the case in the Circuit Court of Appeals is simply a counterpart of the case in the Supreme Court. But the case before us is entirely different. The parties did not treat it as a donation. The city issued the full amount of one hundred thousand dollars in bonds, and the company issued a certificate for one hundred thousand dollars of stock, and until the receipt of this certificate no sale had been made of it. All that the record shows was an agreement on the part of the city to sell at a named price. Nowhere is it shown that the company agreed absolutely to purchase. It was, until after the receipt of the stock, an unaccepted offer on the part of the city. No contract was signed by the company. * * * So far as is disclosed, when the trustee delivered the one hundred thousand dollars in bonds and received the one hundred thousand dollars in stock, there was nothing creating any obligation on the company to repurchase its stock, or to return to the city any portion of the bonds. The city had offered to sell, but it had not agreed to buy. It could have stopped with the receipt of the one hundred thousand dollars of bonds, and left the city to do what it pleased with the stock. There is, therefore, not presented the case of an ignoring of the fact or terms of a

could not maintain an action for money had and received to recover the amount paid to the city for such bonds, as the city having no power to create the debt, no implied promise could arise for its payment, notwithstanding the general statute of Missouri which gives the board of trustees power "to borrow money for the improvement" of the town, the money having been borrowed in violation of the Constitution, and not for the improvement of the town, but to buy a right of way and depot grounds for a railroad.[1]

subscription. Everything authorized by the vote of the people was done, and fully done, and whatever wrong may have been committed by the city council in its proffer of sale and subsequent sale of the stock could not vitiate the bonds after they had passed into the hands of a *bona fide* holder. But, further, the bonds on their face show that they were issued in payment of stock in the railroad company, and recite that they were issued in pursuance of an ordinance of the city council, and authorized by a vote of the citizens and in accordance with the laws of the state; and these were duly registered by the auditor of the state, and his certificate of registry was indorsed on the back. It is true that the recitals do not show when the ordinance was passed or the election held, and do not refer by title or otherwise to the particular statute granting the authority, and the bonds were dated and issued after the Constitution of 1870 had come into force. It is also true that the certificate of registry is not conclusive that the bonds were issued in full compliance with the terms and conditions of a subscription. German Savings Bank *v.* Franklin County, 128 U. S. 526, 540. But surely these recitals and this certificate have significance. It is unnecessary to affirm that the certificates are so 'clear and unambiguous' (School District *v.* Stone, 106 U. S. 183, 187) as to estop the city from showing that the bonds were issued in violation or without authority of law, or that they, in conjunction with the certificate, foreclose all possible defenses. But when the law of the state provides for registry of municipal bonds and a certificate thereof, such certificate should be held as sufficient evidence to a purchaser of the existence of those facts upon which alone bonds can be registered. If the plaintiff in this case, not resting upon the mere terms of the certificate, had examined the records of the auditor's office, he would have found there the certificate, under oath, of the mayor of the city, of the election, its date, and facts necessary to warrant the issue of the bonds, such officer being the one named in the statute as the one to furnish to the auditor the evidence necessary to justify the registry. Can it be that a purchaser, with this evidence before him, is not protected by the statement upon the face of the bonds that they were issued in payment of a subscription? Is it his duty to examine all the proceedings, to see whether that which was a subscription in the first instance was called a subscription all the way through, and was named as a subscription in the bonds, had not been transformed by some action of the city council into a donation? It will be borne in mind that it is not a matter of law, but of fact, in respect to which an estoppel is urged against the city by virtue of the recitals and the fact of registry."

[1] Morton *v.* City of Nevada, (1890) 41 Fed. Rep. 582. See Jarrolt *v.* Moberly, 103 U. S. 586; Litchfield *v.* Ballou, 114 U. S. 190; s. c., 5 Sup. Ct. Rep. 820; Buchanan *v.* Litchfield, 102 U. S. 278.

§ 470. **Miscellaneous rules as to city aid bonds.** — Though properly a city, bonds issued by it under the name of a village will not be rendered invalid as against a *bona fide* purchaser where the legislature has recognized the corporation as a village, and it had acted as such.[1] Where an ordinance of a city regularly passed submitted to a vote of the inhabitants the question of issuing bonds to aid in the construction of a railroad, and the vote taken favoring the proposed aid, the road was constructed according to the terms of the ordinance, the Kentucky Court of Appeals held that the ordinance, without a subsequent contract of subscription, bound the city to issue the bonds.[2] Where an issue of bonds of a municipal corporation had been described in a notice of an election for their issue as "payable in gold or lawful money," as provided by the statute and with interest payable "annually," a subsequent ordinance of the corporate authorities making the bonds payable in gold coin "of the present standard of weight and fineness" with interest "semi-annually" has been held to have rendered the bonds invalid, when questioned before delivery to a purchaser.[3] A statute of Nebraska providing that the auditor shall detach coupons of municipal bonds presented to him for registration which mature before the first taxes levied to meet the coupons, has been held to apply to bonds issued by a city to aid a work of internal improvement.[4] The acceptance of bonds in payment of a subscription of a city to the stock of a corporation which is invalid because unauthorized, will not render the city a stockholder in the corporation.[5]

[1] Cornell University *v.* Maumee, 68 Fed. Rep. 418.

[2] Board of Trustees of Augusta *v.* Maysville & B. S. R. Co., (Ky.) 30 S. W. Rep. 1.

[3] Skinner *v.* City of Santa Rosa, (Cal.) 40 Pac. Rep. 742.

[4] Brinkworth *v.* Grable, (Neb.) 63 N. W. Rep. 952.

[5] City of Geneseo *v.* Geneseo Natural Gas, Coal, Oil, Salt & Mineral Co., (Kans.) 40 Pac. Rep. 655. As to estoppel of municipal corporation to assert lack of authority on the part of its officers in issuing aid bonds as against *bona fide* purchasers, see City of Columbus *v.* Dennison, 69 Fed. Rep. 58.

CHAPTER XXIV.

MUNICIPAL AID BONDS — TOWNS.

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§ 471. **Aid by towns, generally.**— It was held in an Illinois case that it was in the power of the legislature to bestow the power upon a town to subscribe for and take stock in a railroad directly, without requiring the subject to be submitted to a vote of the people.[1] Authority cannot be implied in municipal corporations to incur debts or borrow money in order to purchase stock or subscribe for shares of stock in railroad corporations; it must be conferred by express grant.[2] The power of municipal corporations to subscribe to the stock of railroad corporations and to issue bonds in payment of such subscription in aid of the enterprise must not only be clearly conferred, but the mode prescribed

[1] Keithsburg *v.* Frick, 34 Ill. 405.
[2] Pitzman *v.* Village of Freeburg, 92 Ill. 111.

by the statute conferring the power must be strictly pursued.[1] A clause in a railroad charter to this effect: "It shall be lawful for all persons of lawful age, or for the agent of any corporate body, to subscribe to the capital stock of said company," would confer no power upon municipal corporations to subscribe for such stock.[2] The rights of the holders of bonds of a town in aid of railroads depend upon whether there has in fact been a substantial compliance with the requirements of the law authorizing an election to be held upon the question of subscription and bonds for such purpose.[3] Bonds issued by a township in Kansas by the General Statutes are required to be "signed by the township trustee and attested by the town clerk." It was held in the federal court for that district that the township bonds sued on were not invalidated by the fact that the name of the township trustee was signed for him by a third person in his presence and at his request, the bonds being subsequently duly delivered and certified and the interest paid thereon by the township for ten years.[4] A township having voted aid by taking stock in a railroad company, under the Indiana statutes, the company would have no right to demand the money as a donation.[5] The law of Minnesota as to the issuance of bonds by towns in aid of railroads makes the limit of the indebtedness which may be created five per cent of the assessed valuation as determined by the last assessment. A case before the Supreme Court of that state involved the validity of certain town bonds of this description, it being claimed that the amount of the bonds issued was in excess of this limitation. The court declared that, in determining the amount of such indebtedness, the par value of the bonds was alone to be considered, and not the interest which might subsequently become due thereon

[1] Harding *v.* Rockford, Rock Island & St. Louis R. R. Co., 65 Ill. 90. That legislative authority is necessary for the legal issuance of municipal bonds in aid of railroads, see People ex rel. *v.* Jackson County, 92 Ill. 441; Gaddis *v.* Richland County, 92 Ill. 119; Town of Pana *v.* Lippincott, 2 Bradw. 466; Lippincott *v.* Town of Pana, 92 Ill. 24; Hewitt *v.* Board of Education, 94 Ill. 528; Schaeffer *v.* Bonham, 95 Ill. 368; Pitzman *v.* Freeburg, 92 Ill. 111.

[2] Campbell *v.* Paris & Decatur R. R. Co., (1874) 71 Ill. 311.

[3] Jacksonville, N. W. & S. E. R. R. Co. *v.* Town of Virden, 104 Ill. 339.

[4] Montgomery *v.* Township of St. Mary's, (1890) 43 Fed. Rep. 362. The court cited, as pertinent to their ruling: Ring *v.* County of Johnson, 6 Iowa, 272; Railroad Co. *v.* Marion County, 36 Mo. 303; Just *v.* Wise Township, 42 Mich. 575; s. c., 4 N. W. Rep. 298; Town of Weyauwega *v.* Ayling, 99 U. S. 112, 118.

[5] Board of Commissioners *v.* State 115 Ind. 64; s. c., 17 N. E. Rep. 855.

by the terms of the bonds.[1] In an action by an innocent purchaser against a township on railway aid bonds, which, on their face, refer to the act authorizing their issuance, and specifically recite the taking of each step required thereby, the township is estopped to allege invalidity of the bonds on any ground except that they were issued in violation of some constitutional or statutory requirement.[2] In a case in Illinois where a notice was given that an election would be had on a certain day to vote for and against subscribing an amount authorized by the statutes to the stock of a railroad corporation by the township, and subsequently another notice was given for an election on the same day for another subscription to the same corporation for another sum, the Supreme Court held that both elections were legal, and that one did not invalidate the other.[3] But, as the law authorizing a subscription by the township limited the amount of the subscription to the larger amount voted, the vote of the smaller amount, without any authority, was void and conferred upon the township authorities no power to issue bonds to the railroad corporation. They also held that the proceeding for this additional issue of bonds to the railroad corporation being void, the legislature had no power, under the Constitution, to pass a law rendering the election and subscription valid.[4] Where the power to subscribe to stock on the part of a town is to a particular division of a railroad, it would not be authorized to subscribe to the stock of the whole road.[5] The conditions of subscription and bonds or call for an election to authorize the same must be shown to have been complied with in *mandamus* proceedings to compel the town authorities to issue bonds voted by the town.[6] A suit in equity to restrain the payment of interest upon railroad aid bonds, and to require the bonds to be delivered up and canceled, may be brought by a town without awaiting an action at law upon the bonds, and setting up a defense to the action of the invalidity of

[1] Finlayson *v.* Vaughn, (1893) 54 Minn. 331; s. c., 56 N. W. Rep. 49; Durant *v.* Iowa County, Woolw. 71.

[2] Township of Washington *v.* Coler, (1892) 51 Fed. Rep. 362; citing Chaffee Co. *v.* Potter, 142 U. S. 355–364; s. c., 12 Sup. Ct. Rep. 216; Town of Coloma *v.* Eaves, 92 U. S. 491; Lake Co. *v.* Graham, 130 U. S. 674–681: s. c., 9 Sup. Ct. Rep. 654.

[3] Marshall *v.* Sillman, (1891) 61 Ill. 218.

[4] Ibid.; adhered to in Wiley *v.* Silliman, 62 Ill. 170.

[5] Town of Big Grove *v.* Wells, 65 Ill. 263; McWhorter *v.* People, 65 Ill. 290.

[6] People *v.* Chapman, 66 Ill. 137.

the bonds.[1] Where a township had, upon an election ordered by the public authorities under a mistaken idea of their power, voted for the subscription to the stock of a railroad company and the issuance of bonds in payment of the same, the Supreme Court of Illinois held that taxpayers were entitled to a perpetual injunction restraining the supervisors from issuing such bonds and the railroad company from receiving them.[2] Where the proposition submitted to the voters of a Kansas township containing a condition that if the county became a stockholder in the corporation, or issued bonds to it under any subscription, the subscription of the township was to be null and void, was adopted by the voters of the township at an election properly held under the statute of that state, the Supreme Court held that the subscription by the township was not avoided by the action of the railroad corporation to enforce a pretended subscription of the county and obtain the county bonds therefor, where, on final hearing of the action, the so-called subscription of the county was held invalid for want of power on the part of the county to make it, and no bonds were obtained thereunder.[3] Where the donation of money by a municipal corporation to aid in the construction of a railroad was authorized by law, and it was provided that a tax should be levied to raise the amount to be donated, it was held that the officers of the corporation could not adopt any other mode of paying the same, and that bonds issued by them for the purpose of paying such indebtedness were void.[4] A vote of the people of a town to subscribe to the stock of a railroad company, in the absence of a law authorizing such vote or subscription, will not be binding upon the town.[5] Where a town has authorized the issue of bonds, the signing of the bonds in blank, and leaving them with

[1] Town of Cherry Creek *v.* Becker, 2 N. Y. Supp. 514.

[2] Campbell *v.* Paris & Decatur R. R. Co., (1874) 71 Ill. 611.

[3] Atchison, Topeka & Santa Fe R. R. Co. *v.* Jefferson County, 21 Kans. 309. As to the burden of showing that bonds were authorized by a proper vote of the corporation at an election legally ordered and held, being upon those seeking to compel their issue or asserting their validity, see People *v.* Town of Bishop, 111 Ill. 124. That the issue of bonds or donations in aid of railroads will not be sustained under the power given them by legislative authority without a strict observance of the requirements as to the steps preliminary to an election, see Lippincott *v* Town of Pana, 92 Ill. 24.

[4] Town of Middleport *v.* Ætna Life Ins. Co., 82 Ill. 562; Lippincott *v.* Town of Pana, 92 Ill. 24.

[5] Barnes *v.* Town of Lacon, 84 Ill. 461.

others to hold until the conditions upon which they were voted are complied with by the railroad company, and afterward filling up the blanks, have been held were irregularities which could not prejudice the rights of innocent holders of the bonds.[1] Where the condition of the subscription of a town to the capital stock of a railroad company was that it should be paid upon the completion of the proposed railroad, and at the time the company should run over their track the first locomotive through that township, it was held that the leasing, temporarily, of the road of another company, and running a locomotive over that line through the township was not a compliance with the condition.[2] The law of the state, both constitutional and statutory, bearing upon the power of a municipality to issue bonds, is conclusively presumed to be known to the purchasers of municipal bonds, and the municipality cannot be estopped, by recitals in the bonds, to deny, even as against *bona fide* purchasers, the powers of commissioners appointed by the legislature to issue them.[3] In case a statute

[1] Niantic Savings Bank *v.* Town of Douglas, 5 Bradw. (Ill.) 579. That a consolidation of a road to which aid has been voted by a town with another will not defeat the donation, see Niantic Savings Bank *v.* Town of Douglas, 5 Bradw. (Ill.) 579.

[2] People *v.* Town of Clayton, 88 Ill. 45. That the consolidation of the road of a company which was to be aided by subscription to stock and issue of bonds, with another, would not release the subscription, see Edwards *v.* People, 88 Ill. 340; Town of Pana *v.* Lippincott, 2 Bradw. (Ill.) 466. As to the effect upon the subscription of a change of the route of railroad, see Town of Reading *v.* Wedder, 66 Ill. 80; Alley *v.* Adams County, 76 Ill. 101.

[3] Travelers' Insurance Co. *v.* Township of Oswego, (1893) 55 Fed. Rep. 361. That recitals in bonds as to the authority of officers to issue them where the authority was lacking are not binding upon the municipality issuing them, see Town of Pana *v.* Lippincott, 2 Bradw. (Ill.) 466. As to the power of towns to extend aid to railroad corporations, see Wood *v.* Commissioners of Oxford, 97 N. C. 227; s. c., 2 S. E. Rep. 653; Town of Enfield *v.* Jordan, 7 Sup. Ct. Rep. 358. For a statute that did not authorize aid by a town to a railroad company out of the town's revenue, see Macon & Birmingham R. R. Co. *v.* Gibson, 85 Ga. 1; s. c., 11 S. E. Rep. 442. Town aid bonds held not recoverable in Gilson *v.* Town of Dayton, 8 Sup. Ct. Rep. 66. The issue of such bonds held not authorized in Town of Concord *v.* Robinson, 7 Sup. Ct. Rep. 937. A contract for bonds, under a Kansas statute, limiting the amount to be issued, duly made and accepted by a railroad company, held binding on the township, and upon the performance of the conditions on its part the company held entitled to the bonds, in Chicago, K. & W. Ry. Co. *v.* Comrs., 38 Kans. 597; s. c., 16 Pac. Rep. 828. The bonds issued under what was known as the "Township Aid Act" of Missouri, though the act was held to be unconstitutional, it has been held were proper subjects of com-

authorizing subscriptions in aid of a railroad is silent as to what the petition for and notice of the election shall contain as to the length of time the corporate bonds shall run before their maturity, and the election is called according to law, it will not be essential to the validity of the election that the time when the bonds shall mature should be fixed in the petition for or notice of the election and the vote of the people.[1] Where, in a town meeting attended by a majority of its legal voters, the question of calling an election for the purpose of voting on the proposition of donating the bonds of the town to a railroad company was before it, and the names of freeholders who were willing to sign a petition for such election were called for and publicly announced, and a committee appointed to prepare the petition, which they did, and signed the names of those freeholders to it, it was held that the freeholders having made no objection when their names were so announced, their silence must be construed as an express assent that their names should be signed to the petition by the committee.[2] Where the law under which a vote was taken on the question of a subscription by the municipal corporation to stock of a railroad corporation did not require the vote to be taken in reference to the stock of any particular company, but was in general terms to any railroad corporation leading to or from the town, a vote of a certain sum for railroad subscription, without designating any particular company, has been held to authorize a corporate subscription to the stock of a company whose road passed through the town.[3] It has been held by GRESHAM, United States Circuit

promise, and under the statute authorizing the issue of compromise bonds subsequently passed, the tax levied to pay them was held to be valid. State *v.* Hannibal & St. Joseph R. R. Co., (Mo.) 11 S. W. Rep. 746. The Iowa statute requires that the notice of an election to raise a tax for a railroad shall show to what point the road shall be fully completed before the tax shall become due. Kleise *v.* Galusha, 78 Iowa, 310; s. c., 43 N. W. Rep. 217, following Allard *v.* Gaston, 70 Iowa, 731; s. c., 29 N. W. Rep. 752. Notice, simply stating that the tax shall become due on the completion of a certain number of consecutive miles of the road in a certain township by a specified time was held to be insufficient, and the tax voted at the election held to be void.

[1] People *v.* Town of Harp, 67 Ill. 62.

[2] Chicago, D. & V. R. R. Co. *v.* Coyer, 79 Ill. 373.

[3] Decker *v.* Hughes, 68 Ill. 33. When there is no power to compel the issue of bonds, see Springfield & I. S. E. Ry. Co. *v.* Cold Spring Township, 72 Ill. 603. An election for town aid bonds held invalid and not to have conferred authority for their issue. Harmon *v.* Auditor of Public Accounts, 22 Ill. App. 129; affirmed in 123 Ill. 122; s. c., 13 N. E. Rep. 161. When

Judge, that, under the Illinois decisions denying interest on the overdue interest coupons of railroad aid bonds, such interest was not recoverable in the federal courts.[1] There was a provision in a charter of a railroad company in Illinois authorizing the voting of municipal subscriptions for its stock, that the bonds should not be issued, nor any payment made on the subscription, until an amount of work shall be done on the railroad in the town, or on such part of the line of the road, as the authorities of the town shall designate, equal in value to the amount of the bonds to be issued. It was held that the charter required any deviation from the conditions therein prescribed to be submitted to the voters,

an election was held illegal and not to confer authority to make a subscription. People *v.* Town of Santa Anna, 67 Ill. 57; People *v.* Town of Lacuna, 67 Ill. 65; Town of Pana *v.* Lippincott, 2 Bradw. (Ill.) 466; Lippincott *v.* Town of Pana, 92 Ill. 24. That the legislature may legalize and declare valid bonds issued by a town in aid of railroads without authority to do so, see Town of Keithsburg *v.* Frick, 34 Ill. 405.

[1] Bolles *v.* Town of Amboy, (1891) 45 Fed. Rep. 168. Issue of town aid bonds held unconstitutional in People *v.* Town of Bishop, 111 Ill. 124. Town aid bonds held unauthorized by reason of defective petition. Rich *v.* Town of Mentz, 134 U. S. 632; s. c., 10 Sup. Ct. Rep. 610. That bonds were issued upon the condition that the railroad company should build its shops in a town, held not to invalidate them in Casey *v.* People, 132 Ill. 546; s. c., 24 N. E. Rep. 570. Where a clerk of a town failed to record a provision of the vote of the town granting aid to a railroad, that the road should be completed by a certain date, an amendment of the record subsequently to the completion of the road, though the completion was after the date named in the condition, was not allowed to defeat the claim of the railroad company to the aid voted, in Sawyer *v.* Manchester & Keene R. R. Co., 62 N. H. 135. In Purdy *v.* Lansing, (1888) 128 U. S. 557, the bonds of this New York town, issued in aid of a certain railroad company, were held to have been issued without authority of law, and to be invalid on the ground that they had been issued without a previous designation by the company of all the counties through which the extension, authorized by the statute of New York relating to it, would pass. As to what was required by the statutes of New York, as to aid by towns preliminary to its being granted, see People *v.* Van Valkenburgh, 63 Barb. 105. Bonds of a town in aid of a railroad under New York statutes held void because of the omission of certain statements in the petition of taxpayers to the county judge, in Strang *v.* Cook, 47 Hun, 46. When a suit to cancel such bonds is not barred. Ibid. When a town was held entitled to a decree for the surrender and cancellation of its bonds in excess of the amount of aid authorized, obtained from the state treasurer on a false certificate of a town trustee that the conditions on which they were issued had been complied with, see Wilson *v.* Union Savings Assn., 42 Fed. Rep. 421. Payment of a tax voted in aid of a railroad by a township held not enforceable in Cantillon *v.* Dubuque & N. W. R. R. Co., (Iowa) 35 N. W. Rep. 620.

and at the election at which the subscription was voted, and that the town authorities could not, at pleasure, make any change as to the part of the road upon which the requisite amount of work should be expended.[1] The town in this case having voted a subscription to be paid in bonds to the amount of $50,000, the court held that the building of the road through the town at a cost of only $30,000 or even $41,000 was not a substantial compliance with the conditions, and that the court would not by *mandamus* compel the issue of the bonds voted.[2] Where the voters of an Illinois town had voted in favor of a proposition to make a donation in aid of a railroad, for which a tax was to be levied and the money paid to the railroad company, the Supreme Court of that state held that the proposition upon which they voted was entirely distinct from one to create a debt in respect to such donation, and a vote of that character would not be construed to authorize the issue of the bonds of the town for the amount so stated.[3] The words of a statute giving the right to prescribe the conditions upon which such subscriptions should be made or bonds issued, and declaring that such subscriptions or bonds should not be valid and binding until such conditions shall have been complied with, it has been held, by their natural force, extended to bonds under all circumstances, in whosesoever hands they might be.[4] Where a town has imposed conditions upon its subscription to stock, etc., of a railroad company, the supervisor of the town, on making the subscription, would have no power to disregard such conditions, nor would the railroad company have any right to demand that he should disregard them.[5] The conditions upon which a municipal subscription may have been valid in aid of a railroad, without express legislative authority, cannot be changed by a subsequent vote, either directly upon the proposition or indirectly upon a proposition to make a donation of a small sum with new conditions as to the donation and the issuing of bonds under the prior vote.[6]

§ 472. Bonds invalid unless conditions are complied with. — It was provided in the act passed April 16, 1869, in Illinois, that

[1] People *v.* Town of Waynesville, 88 Ill. 469.

[2] Ibid.

[3] Schaeffer *v.* Bonham, 95 Ill. 368.

[4] Town of Eagle *v.* Kohn, 84 Ill. 292; Parker *v.* Smith, 3 Bradw. (Ill.) 356.

[5] People *v.* Dutcher, 56 Ill. 144; People *v.* Holden, 91 Ill. 446.

[6] People *v.* Town of Waynesville, 88 Ill. 469.

"any county, township, city or town shall have the right, upon making any subscription or donation to any railroad company, to prescribe the conditions upon which such bonds, subscriptions or donations shall be made, and such bonds, subscriptions or donations shall not be valid and binding until such conditions precedent shall have been complied with." In an action upon interest warrants attached to bonds issued under this act in aid of a railroad, the defense of the town was a failure on the part of the railroad company to comply with some of the conditions upon which the bonds were issued. The trial court sustained a demurrer to the plea of the town. The Supreme Court of the state reversed the lower court, holding that the demurrer should have been sustained; that by virtue of the express declaration of the statute the bonds in question were not valid and binding until the conditions named had been complied with, even in the hands of innocent holders without notice.[1]

[1] Town of Eagle *v.* Kohn, (1876) 84 Ill. 292. *Arguendo*, it was said: "We do not think it is to be regarded that the conditions named were prerequisite to the making of the subscription and issuing of the bonds, and that they were to be complied with before the subscription could be made or the bonds issued; but only that the subscription and the bonds were to be subject to the conditions. There would then be no want of power to make the subscription and issue the bonds. As between the town and the railroad company, non-compliance with the conditions would be a good defense against the railroad company. But, irrespectively of the [provision of the act referred to above] we consider that it would be otherwise as against innocent holders for value, as are these appellees. It is the well-settled doctrine that bonds of this character are to be treated as commercial paper, and this court has held the coupons attached to them to be negotiable by delivery only, without indorsement. Johnson *v.* County of Stark, 24 Ill. 75. And, aside from the provision of the statute, we do not consider that *bona fide* holders for value would be required to take notice of such conditions, or the resolution upon the records of the railroad company, but they would enjoy the protection of *bona fide* holders of negotiable paper; and want of compliance with such conditions or resolution would not constitute any defense against them. * * * The words of the statute, by their natural force, apply to bonds under all circumstances, in whosesoever hands they may be. Courts are wont to allow to such peremptory language of a statute full force and effect, and where a statute expressly declares that negotiable securities, given under certain circumstances, shall be void, to hold them void, even in the hands of a *bona fide* indorsee. Thus, upon the English Statutes of Anne, declaring that promissory notes and bills of exchange, given for an usurious consideration, or for a gaming consideration, should be void, the English courts put the construction that the securities were void in the hands of a *bona fide* indorsee without notice. And so this

§ 473. **How irregularity of election affects the validity of bonds.**— It was insisted in a case before the United States Supreme Court that the township bonds upon which the suit was brought were invalid because of the irregularity of the election to ascertain the will of the legal voters in the matter of a subscription to the stock of the railroad company, in two respects: (1) Because a majority of the legal voters of the township did not vote at the meeting notified and held for that purpose; (2) because the meeting was notified and held before the act was passed providing for such an election. The court held that the true intent of the legislature in adopting the phrase "a majority of the legal voters of the township," intended to require only a majority of the legal voters of the township voting at the election notified and held to ascertain whether the proposition to subscribe for the stock of the company should be adopted or rejected.[1] The court also held that the second objection was not a good one for the reason that the statute by its terms cured

court has held, under our statute in respect to a bill of exchange for a gaming consideration. Chapin et al. *v.* Dake, 57 Ill. 296. And the doctrine is laid down generally that in those cases in which the legislature has declared that the illegality of the contract shall make the security, whether bill or note, void. the defendant may insist on such illegality, though the plaintiff took the bill or note *bona fide*, and gave a valuable consideration for it. Chit. on Bills, 115, and cases cited in note. But, unless it has been *so expressly* declared by the legislature, illegality of consideration will be no defense in an action at the suit of a *bona fide* holder, without notice of the illegality, unless he obtained the bill or note after it became due. Chit. on Bills, 116. True, there is nothing of illegality in the bonds in question, nor does the statute declare them void. But illegality is not the circumstance which avoids negotiable securities in the hands of a *bona fide* holder, as it is seen that illegality of consideration, in the absence of express declaration by the legislature that the securities shall be void, will be no defense against a *bona fide* holder without notice of the illegality. It is by force of the peremptory words of the statute declaring them void, that they are to be held to be void in the hands of an innocent indorsee without notice. The words of the statute in question, though not that the bonds shall be void, are that they shall not be valid and binding until the conditions are complied with. They are equally imperative to the degree named as language declaring securities void. The bonds are not declared to be, to their whole extent, not valid and binding, but *are* declared to be to a certain extent, not valid and binding; that is, until the conditions are complied with."

[1] See on this point, People *v.* Warfield, 20 Ill. 163; People *v.* Garner, 47 Ill. 246; People *v.* Wiant, 48 Ill. 263; Railroad *v.* Davidson County, 1 Sneed, 692; Bridgeport *v.* Railroad, 15 Conn. 475; Talbot *v.* Dent, 9 B. Mon. 526; State *v.* The Mayor, 37 Mo. 272.

all defects growing out of any irregularities as to the election, and, if not, that the act in one of its sections made it the duty of the supervisor who executed the bonds to determine the question whether an election was held, and whether a majority of the votes cast were in favor of the subscription, and inasmuch as he passed upon that question and subscribed for the stock and subsequently executed and delivered the bonds, it was too late to question the validity where it appeared, as in this case, that the bonds were in the hands of an innocent holder.[1] The United States Supreme Court held in a case that an irregularity in conducting the election would not defeat a recovery on the bonds or on the coupons thereto attached, nor overcome the presumption that the plaintiff, in the usual course of business, became at their date the holder of them for value; that the burden of proving that he was an innocent holder of the bonds for value was not cast upon him by such an irregularity in conducting the election.[2]

[1] St. Joseph Township *v.* Rogers, (1872) 16 Wall. 644. See Knox County *v.* Aspinwall, 21 How. 544; Supervisors *v.* Schenck, 5 Wall. 783. The same principles were applied in Royal British Bank *v.* Turquand, 5 Ell. & Bl. 259; s. c., 6 Ell. & Bl. 331.

[2] Pana *v.* Bowler, (1882) 107 U. S. 529. It was said: "It is a general rule that when the holder of a negotiable instrument, regular on its face and payable to bearer, produces it in a suit to recover its contents, and the same has been received in evidence, there is a *prima facie* presumption that he became the holder of it, for value at its date, in the usual course of business. Murray *v.* Lardner, 2 Wall. 110; Bank of Pittsburg *v.* Neal, 22 How. 96; Collins *v.* Gilbert, 94 U. S. 753; Brown *v.* Spofford, 95 U. S. 474. And municipal bonds, payable to bearer, are subject to the same rules as other negotiable paper. Cromwell *v.* Sac County, 96 U. S. 51. But the plaintiff in error insists that this case falls within an exception to that rule, and cites to sustain his position Smith *v.* Sac County, 11 Wall. 139, and Stewart *v.* Lansing, 104 U. S. 505. The exception relied on by the plaintiff in error is well settled, and is this: If, in a suit brought by the indorsee or transferee of a negotiable instrument, the maker or acceptor, or any party who is primarily bound by the original consideration, proves that there was fraud or illegality in the inception of the instrument, the burden of proof is thrown on the plaintiff to show that he is a holder for value. Smith *v.* Sac County, 11 Wall. 139, and Stewart *v.* Lansing, 104 U. S. 505; Commissioners *v.* Clark, 94 U. S. 278 [and many others]. In most of the cases above cited the defense relied on was fraud in the inception of the instrument. Thus, in Smith *v.* Sac County, 11 Wall. 139, the report shows that the bonds were issued to a contractor to pay for the building of a court house; that the county judge who executed and delivered them was bribed to do so, and that the court house never was built. In Stewart *v.* Lansing, 104 U. S. 505, the county judge rendered a

§ 474. **Effect of recitals on face of bonds.**—In an action upon coupons of township bonds, issued by a township in Illinois in payment of a subscription to the capital stock of a railroad company under certain acts of the legislature incorporating this railroad company, the Supreme Court of the United States reaffirmed its ruling in Harter *v.* Kernochan, 103 U. S. 562, that the duly signed and countersigned township bonds, payable to the company or bearer, which recited that they were duly issued in compliance with the vote of the legal voters of the township, cast at an election held by virtue of those acts of the legislature, were valid in the hands of a *bona fide* holder.[1]

judgment appointing commissioners to execute bonds of the town of Lansing. This judgment was carried by *certiorari* to the Supreme Court and there reversed. The county judge, the commissioners and the railroad company to which the bonds were ordered to be issued, all had notice of the *certiorari* and the subsequent proceedings under it. Before the judgment of reversal, however, the commissioners, notwithstanding the pendency of the writ, issued the bonds in suit in the case, taking from the company an obligation for their personal indemnity. The court held that as between the company and the town the judgment of reversal was equivalent to a refusal by the county judge to make the original order and invalidated the bonds. There is no pretense of any fraud in the inception of the bonds in this case. It is not denied that they were issued in good faith and for a valuable consideration. The question then arises: Is the irregularity in the conduct of the election such an illegality as throws on the plaintiff the burden to show that he paid full value for the coupons? We are clearly of opinion that it is not. It will appear from an examination of the cases above cited, in which the defense was illegality in the inception of the instrument, that the illegality which shifts the burden of proof on the holder to prove that he paid value must be something which relates to the consideration of the paper sued on. It must appear that the consideration arose out of a transaction contrary to law, or against public policy." The court then commented upon certain of the cases and summed up, on this point, in the following words: "The authorities illustrate the rule and show that it does not apply to this case. There was no illegality whatever in the consideration of the bonds in question in this suit. The mere irregularity in the conduct of the election was not such an illegality as is contemplated by the rule, and does not deprive the holder of the coupons of the presumption that he acquired them for value."

[1] Pana *v.* Bowler, (1882) 107 U. S. 529. Mr. Justice Woods, speaking for the court, said: "This court has again and again decided that if a municipal body has lawful power to issue bonds or other negotiable securities, dependent only upon the adoption of certain preliminary proceedings, such as a popular election of the constituent body, the holder in good faith has the right to assume that such preliminary proceedings have taken place if the fact be certified on the face of the bonds by the authorities whose pri-

§ 475. **The power of commissioners of towns for issuing aid bonds under New York statutes.**— The Court of Appeals of New York has held that the acts of commissioners appointed to execute and issue the bonds in the proceedings under the statutes of that state authorizing the issuing of bonds by towns in aid of railroads, as to all matters within the scope of the authority

mary duty it is to ascertain it. Lynde *v.* The County, 16 Wall. 6; Town of Coloma *v.* Eaves, 92 U. S. 484; Commissioners *v.* January, 94 U. S. 202; Commissioners *v.* Bolles, 94 U. S. 104; County of Warren *v.* Marey, 97 U. S. 96. The authority to issue the bonds in question in this case, resting upon the fact that an election was held in pursuance of law before a certain date, namely, the date when the Constitution of 1870 was adopted, and the bonds reciting on their face the fact that the election was so held before the date mentioned, the circumstance that the election was irregularly conducted can be of no avail as a defense to the bonds in a suit brought by a *bona fide* holder." The court's attention was called to several Illinois decisions (Lippincott *v.* Town of Pana, 92 Ill. 24), in which it was held that the election relied on in this case as the authority for the issue of the bonds was absolutely void, and the issue of the bonds was, therefore, without authority. People *v.* Town of Santa Anna, 67 Ill. 57, and People *v.* Town of Laenna, 67 Ill. 65, where similar elections under a like statute were held void. The court said of these cases: "The last two cases were decided before the bonds in this case were issued. They were, however, suits brought to restrain the issue of bonds by the township officers, on account of the irregularities in the election. The rights of *bona fide* holders could not, therefore, arise and were not passed on in those cases. But in the case first mentioned the bonds had been issued and were presumptively in the hands of *bona fide* holders. Nevertheless, the Supreme Court of Illinois held the bonds to be void in whosesoever hands they might be. It is insisted that this court is bound to follow this decision of the Supreme Court of Illinois and hold the bonds in question void. We do not so understand our duty. Where the construction of a State Constitution or law has become settled by the decision of the state courts, the courts of the United States will, as a general rule, accept it as evidence of what the local law is. Thus, we may be required to yield against our own judgment to the proposition that, under the charter of the railway company, the election in this case, which was held under the supervision of a moderator chosen by the electors present, was irregular and, therefore, void. But we are not bound to accept the inference drawn by the Supreme Court of Illinois, that in consequence of such irregularity in the election the bonds issued in pursuance of it by the officers of the township, which recite on their face that the election was held in accordance with the statute, are void in the hands of *bona fide* holders. This latter proposition is one which falls among the general principles and doctrines of commercial jurisprudence, upon which it is our duty to form an independent judgment, and in respect of which we are under no obligation to follow implicitly the conclusions of any other court, however learned or able it may be. Swift *v.* Tyson, 16 Pet. 1; Russell *v.* Southard, 12 How. 139; Watson *v.* Tarpley, 18 How. 517; Butz *v.* City of Muscatine, 8 Wall. 575; Boyce

conferred upon them by the statutes, are the acts of the town.[1] Further, it was held that irregularities in the manner in which such commissioners may have performed their duties could not affect the validity of the bonds in the hands of an innocent holder for value.[2] The court further held that the employment by the commissioners of the president of the railroad company, to the stock of which the town had subscribed and was to issue its bonds in payment of the subscription, who was a banker, as a broker to sell the bonds and invest the proceeds according to their instructions, was allowable under the law.[3] The lawfully appointed broker for the commissioners who issued the town bonds in this case sold bonds to an amount less than ten per cent of the amount authorized to a purchaser, who brought his action against the town. The original act authorizing these railroad aid bonds by towns provided for bonds running thirty years. This portion of the act was afterwards amended, as follows: "The said commissioners may issue the said bonds, payable at any time they may elect, less than thirty years, * * * but they shall not so issue the bonds that more than ten per cent of the principal of the bonds shall become due and payable in one year." The bonds sued on were twenty-year bonds. The town objected to a recovery upon these bonds, claiming that there was no authority when they were issued to issue bonds for twenty years, they being of date prior to the passage of the amendatory act, and that if the

v. Tabb, 18 Wall. 546; Oates *v.* National Bank, 100 U. S. 239; Railroad Company *v.* National Bank, 102 U. S. 14. See, also, Burgess *v.* Seligman, 107 U. S. 20, where the question how far the courts of the United States are bound by the decisions of the state courts is carefully re-examined and the rule on the subject stated with precision." It was further said: "We cannot follow the decision of the Supreme Court of Illinois in Lippincott *v.* Town of Pana, 92 Ill. 24, without overruling a uniform current of the decisions of this court beginning with Commissioners of Knox County *v.* Aspinwall, 21 How. 539, and continuing down to the present time. The rights of the *bona fide* holders of negotiable municipal bonds, as we have stated them in this opinion, are too firmly settled by the decisions of this court to be shaken."

[1] Brownell *v.* Town of Greenwich, (1889) 114 N. Y. 518; citing Gould *v.* Town of Oneonta, 71 N. Y. 298.

[2] Brownell *v.* Town of Greenwich, (1889) 114 N. Y. 518; citing Town of Solon *v.* Williamsburgh Savings Bank, 114 N. Y. 122.

[3] Brownell *v.* Town of Greenwich, (1889) 114 N. Y. 518. The court said: "It was not necessary that merely executive acts, not involving the exercise of discretion, should be done by the commissioners personally, but such acts might be done by another under their direction. Mayor *v.* Sands, 105 N. Y. 210, 217. When a statute com-

amendatory act was operative then there was a violation of the limitation of that act with reference to the amount of bonds which can be made payable in one year. The Court of Appeals of New York held that the bonds were valid obligations of the town, and enforceable by the owner or *bona fide* purchaser for value.[1] A certain amount of the bonds of this town which had

mands an act to be done it authorizes all that is necessary for its performance."

[1] Brownell *v.* Town of Greenwich, (1889) 114 N. Y. 518. The court said: "[The bonds] bear the date [prior to the passage of the amendatory act], and are presumed to have been executed at that time; but executing is not issuing, for they might be fully executed but never issued. It is clear that the purchaser of a bond from the obligor named therein simply lends the latter money. Coddington *v.* Gilbert, 17 N. Y. 489; Ahern *v.* Goodspeed, 72 N. Y. 108. The essence of the original transaction between the parties, therefore, was a loan of money secured by the bonds of the borrower. The bonds had no legal inception, and could not become valid obligations, aside from any other question, until actually delivered for a valuable consideration. Under the circumstances, we think that the delivery of the bonds to the plaintiff determines the date when his bonds were issued. In this vital respect the case differs from Potter *v.* Town of Greenwich, 92 N. Y. 662; 26 Hun, 326, where the bonds were issued prior to the passage of the [amendatory] act. * * * The plaintiff in that case bought his bonds [prior to that date]." The bonds here were purchased July 1, 1871, after the passage of the amendatory act. The court said of them: "[They] were issued on [the date of purchase], when they were first delivered as evidence of an existing debt. The plaintiff had the right to assume that they were issued under the statute as it stood at the date of delivery, for he was dealing with actual commissioners, clothed with all the authority that the state conferred. The mere inspection of his bonds would show that *they* were made payable as the statute then required. It does not appear that he had seen any of the bonds except those which he purchased, or that he knew that all of the bonds were payable at the same time, or even that any other bonds had been issued at the date of his purchase. He was not bound to examine the entire series to see that no more became due in a single year than the statute permitted. He was bound to examine his own bonds, and was, doubtless, charged with knowledge of the bonding act and the bonding roll, as the one was a public statute and the other a public record, and both were accessible to all. How could he examine the remaining bonds? If they were not then issued, but still in the hands of the commissioners, an examination would be useless, for a purchaser of bonds issued according to law, cannot be affected by the subsequent acts of the commissioners in issuing other bonds in a manner not in accordance with law. If they were issued, how could he find them, scattered in the hands of unknown owners? It would be unreasonable to charge him with knowledge of the contents of the rest of the bonds, or to declare his bonds void because the others, of which he knew nothing and had no means of knowing, were, in fact, made payable at a time not authorized by the statute. A purchaser, under the circumstances disclosed, might assume

been issued in aid of a railroad company in a proceeding under the New York statutes providing for and authorizing such bonds, had been returned to the commissioners appointed to execute and issue them and other bonds, to the same amount substituted by the commissioners, larger in amount, severally, and payable at a different place, which, it was assumed, would make them more salable. In the town's action against the bank which held some of these bonds, to have them surrendered and canceled, one of the grounds upon which they were claimed to be invalid was that there was no authority in the commissioners to substitute these bonds for the others. The Court of Appeals held that the commissioners had the power to substitute the bonds last issued for those surrendered to them by the holders, and that the substituted bonds were not invalid.[1]

that the defendant, through its lawfully appointed commissioners, would not do an act utterly void, and thereby commit a fraud upon one of its citizens by taking his money without any consideration."

[1] Town of Solon *v.* Williamsburgh Savings Bank, (1889) 114 N. Y. 122. The court said: "The bonds issued pursuant to the statute were the obligations of the town, and in the performance of their defined duty in that respect, the commissioners represented the [town], and, in some sense, their relation was that of agency. When the proceeding for the purpose has been (as is treated to have been in this case) legally conducted to the appointment of such officers, irregularities in the manner in which they perform their duties do not affect the validity of the bonds issued in the hands of an innocent holder for value. Town of Lyons *v.* Chamberlain, 89 N. Y. 586. The bonds are in form negotiable, and while they cannot be treated as commercial paper, to the extent of the rule applicable to it in that respect, they have the character of negotiability sufficient to furnish, under some circumstances, protection to a *bona fide* holder, which he otherwise would not have for the support of his claim upon them. Bank of Rome *v.* Village of Rome, 19 N. Y. 20; Brainerd *v.* N. Y. C. R. R. Co., 25 N. Y. 499. The liability of the municipal corporation is dependent upon the statute, and its observance in the proceedings had with a view to the creation of such obligations. And when there is a failure to comply with the statute in the steps taken to vest the power in those officers to create the bonds, there can in this state be taken no rights by a person as a *bona fide* holder. Cagwin *v.* Town of Hancock, 84 N. Y. 532; Craig *v.* Town of Andes, 93 N. Y. 405. So far as we have observed, the doctrine of the cases does not necessarily go any further in that respect. The examination of the proceedings before the county judge disclosed their regularity and showed that the persons whose names were subscribed to the bonds were only appointed, and by the statute vested with the power to issue bonds like those in question. While the commissioners were not appointed by the town or clothed with power by it, the power to exercise their statutorily defined duties was given pursuant to the requisite consent of the taxpayers. The question, therefore, arises whether, by this issue of the substituted bonds, the [town]

The Constitution of the state of New York which went into effect January 1, 1875, declared: "No county, city, town or village shall hereafter give any money or property, or loan its money or credit, to or in aid of any individual, association or corporation, or become directly or indirectly the owner of stock in, or bonds

was charged with liability. The issue of bonds outstanding in excess of the amount authorized would have been void. That was not the case here, and the [town] was practically unaffected by those put in place of the ones surrendered. The [town], through the commissioners, paid the interest coupons upon them for several years, and the defendant was the holder of them for six years before this action was commenced. These facts might be entitled to some consideration upon the question of *laches*. Alvord *v.* Syracuse Sav. Bank, 98 N. Y. 599, 610. But we do not place our conclusion upon that ground. The defendant was a *bona fide* holder of these bonds, and as such relied upon the authority with which the commissioners were lawfully clothed. To charge the [town] upon them would not increase its apparent liability beyond that which it undertook by the proceeding had pursuant to the statute to assume. So there is no equity in its behalf as against the defendant, to support this action for their cancellation arising out of the substitution. The defendant was, not only by the apparent situation at the time of the purchase, but by the continued recognition of the obligation of the bonds for several years thereafter, induced to understand that they were in all respects lawfully created. And they were, in fact, issued and delivered by the persons clothed with power to issue the bonds of the town. The extrinsic fact now relied upon to deny to them the power to issue these particular bonds at the time and in the manner it was done, was peculiarly within the knowledge of those persons so selected to represent the town in that respect. This, as between principal and agent, is sufficient to charge the former with the consequences of the act of the latter in the scope of his apparent authority, as against an innocent party acting in reliance upon such situation, although authority to do the particular act does not, in fact, exist. N. Y. & N. H. R. R. Co. *v.* Schuyler, 34 N. Y. 30; Bank of Batavia *v.* N. Y., L. E. & W. R. R. Co., 106 N. Y. 195. This proposition may not, to the full extend to which it is applied to the relation of an agent clothed by his principal with authority, be applicable to the commissioners in their relation to the town for which they are appointed to perform the duties devolved upon them, but in the reason of it is illustrated a principle which may be applied to the circumstances of the present case in reference to the execution of the bonds in question. In the cited case of Horton *v.* Town of Thompson, 71 N. Y. 513, the bonds appeared to have been, in terms, issued in violation of the statute pursuant to which the consent of the taxpayers was given, upon which the proceeding taken was had. And the remarks of the learned judge who delivered the opinion may be treated as applicable only to the case as there presented. They represent the town in the exercise of the powers with which they are vested. Cagwin *v.* Town of Hancock, 84 N. Y. 542; Alvord *v.* Syracuse Savings Bank, 98 N. Y. 599. The practical effect of this subscription of the bonds was not an excessive issue, but the continuance

of, any association or corporation, nor shall any such county, city, town or village be allowed to incur any indebtedness except for county, city, town or village purposes." A town of New York had, previously to the adoption of this amended Constitution, in proceedings instituted under the acts of the state relating to such matters, determined to issue its bonds in aid of a railroad company. The act of 1870 authorized the commissioners of the town appointed in such proceedings and the railroad company to enter into an agreement for limiting and defining the times when and proportions in which the bonds should be delivered, and the places where and the purposes for which they should be applied. It also provided that "the petition" [of the taxpayers] may be absolute or conditional, and, if the same be conditional, the acceptance of a subscription founded on such petition shall bind the railroad company accepting the same to the observance of the condition or conditions specified in such petition. The petition in this case was for authority to issue bonds to a certain amount to a certain railroad company, conditioned that its road be constructed from a certain point to a certain other point and to pass through a certain village in this town. The commissioners of the town just afterwards, the issue of the bonds having been authorized, entered into an agreement with the railroad company to deliver the bonds when those conditions, referring to the petition, on the part of the railroad company were performed. In a statutory proceeding, upon an agreed statement of facts, before the Supreme Court of the state of New York, after the adoption of the amended Constitution, in which the railroad company prayed for an order directing the issue of the bonds and the subscription of the stock, and the commissioners prayed for a decree against such issue and subscription, the decree was made as prayed by the commissioners. This was affirmed by the Court of Appeals of that state. The Court of Appeals held that there was no contract in existence, as alleged by the railroad company, when the amended Constitution went into effect, and, therefore, that the

of those issued, modified in form, not in substance, and these were the only ones, with others outstanding, which covered the amount of the stock of the railroad company, to which the commissioners had subscribed for the town, and for which they had undertaken to issue its bonds for a like amount." The case of The Town of Solon *v.* Williamsburgh Savings Bank, (1889) 114 N. Y. 122, was thoroughly discussed and its conclusions adhered to in Williamsburgh Savings Bank *v.* Town of Solon, (1893) 136 N. Y. 465.

prohibition contained in the Constitution before quoted was conclusive against the right and power of the town to issue the bonds and subscribe for the stock which formed the subject of this litigation. A writ of error was taken to the United States Supreme Court upon the constitutional question involved, and they considered whether any such contract, valid and binding on this town, did exist at the time of the adoption of the amended Constitution. In the opinion rendered in the case by the United States Supreme Court Mr. Justice BRADLEY, speaking for the court, made this statement of the facts, that "the railroad was not constructed through [the village named in the petition and agreement before referred to] until the 20th of October, 1875. On the 1st of January, 1875, when the amended Constitution went into effect, nothing had been done except to survey the route and file a map thereof." The court affirmed the decision of the New York Court of Appeals, holding the agreement made by the commissioners with the railroad company *ultra vires* and not binding upon the town.[1]

[1] Railroad Company *v.* Falconer, (1880) 103 U. S. 821. It was said, as to the power of these commissioners in the matter: "Their powers were confined to subscribing for the stock and making and issuing the bonds in payment thereof when and as the petition of the taxpayers directed; that is, after the road was completed through [the village in the town]. By the act of 1870 they might also stipulate as to the installments in which the bonds should be delivered, and the purposes for which they might be applied. But the power to do this being but an incident of the principal power to make and issue the bonds, and being only intended to enable the commissioners to prescribe the times and manner of their issue and the uses to which they should be applied, would not properly arise and could not be effectively exercised until the principal power itself arose and became exercisable. Whilst, however, the commissioners had the power, or, rather, would have the power, at the prescribed time, to subscribe for the stock and to execute and issue the bonds, neither the statutes nor the taxpayers' petition gave them any power to make a contract to subscribe for stock, nor a contract to deliver bonds to the railroad company. They were not charged with any such duty; they were not invested with any such power. The case of the railroad company, therefore, must stand upon the effect of the taxpayers' petition and the proceedings had thereon before the county judge. If, under the operation of existing statutes, these proceedings amounted to a contract between the town and the railroad company, no subsequent legislation or constitutional amendment could lawfully impair its obligation. But it is difficult to see how said petition and proceedings, including the appointment of commissioners, can be considered as amounting to such a contract. All that was done by the town, through the action of its taxpayers and the county judge, was to appoint agents for making a subscription and issuing

§ 476. **The sealing of such bonds.**— A town of New York issued bonds in aid of a railroad corporation. The town had no common seal. The attestation clause of each bond was: "In witness whereof the within named commissioners * * * have caused this bond to be made and executed and have set their hands and seals hereto the first day of ——— in the year ——;" and they subscribed their names as commissioners, and opposite each name was the scroll [L. S.]. In an action by the town against a bank, the holder of these bonds, praying that they be

bonds on the happening of a certain event. When that event should happen it would be the duty of these agents, under [a] section of the act of 1869, to execute their commission. The words of the section are: 'Such commissioners are further empowered and *directed* to subscribe,' etc. But to whom did they owe this duty? Evidently to the town which appointed them; not to the railroad company. The latter came under no obligation and acquired no rights until the commissioners should subscribe to its stock. Had no conditions been imposed by the petition, the duty of the commissioners to subscribe stock and issue bonds would have arisen immediately after their appointment; but it would have been an obligation owed to their principals alone. The conditions which were in fact imposed required, it is true, something to be done by the railroad company before the commissioners could act; but no stipulation was demanded of the company, or given by it, that this something should be done. The two parties were not brought together. There was no mutuality between them. Each was free to act as it listed. This was the condition of things on the 1st of January, 1875, when the new Constitution went into operation, prohibiting all municipal aid to corporations or individuals, by subscription of stock or otherwise. It seems to us, therefore, that the New York Court of Appeals was right in deciding that no contract existed at that time. After the amendment took effect, no county, city, town or village could subscribe for railroad stock; and, of course, no agent or attorney of any such corporation could do so. What had not been done before, in this regard, could not be done afterwards, unless some valid contract required it to be done. But, as we have shown, no such contract existed in this case, The action on the part of the town was voluntary up to the time of the constitutional amendment. The railroad company may have expected a subscription when their road should be completed; but they had no subscription, and had no valid agreement that any should be made. Everything was inchoate and undetermined up to the first day of January, 1875, and then all power to subscribe for stock was taken away from the town." County of Moultrie *v.* Savings Bank, 92 U. S. 631, was relied upon to sustain the position that a contract did exist in this case. It was distinguished by the United States Supreme Court as follows: "But an examination of that case will show that it was very far from being parallel to the present. Here the statute of Illinois authorized the board of supervisors of the county of Moultrie to subscribe to the stock of a particular railroad company by name, to an amount not exceeding eighty thousand dollars, and to issue bonds therefor when the road

surrendered and canceled, it being claimed that they were invalid on account of the manner in which they had been executed and sealed by these commissioners appointed in the proceedings before a county judge under the New York statutes to execute and issue them to the railroad company, the Court of Appeals, while conceding that the doctrine established in that state did not permit the conclusion that the seal upon the bonds in question was the seal of the commissioners, held that it did not follow that the bonds were for that reason invalid, and inasmuch as they were issued and delivered by the commissioners in the performance of their duty, and upon a consideration, the mistake or failure to affix their seals did not defeat the enforceable validity of the bonds.[1] At the time the bank became the holder and owner of

should be opened for traffic between certain points. Before this event took place, the board ordered that a subscription to the stock of the company in the sum of eighty thousand dollars be made, and that, in payment therefor, bonds should be issued to the company when the road should be open for traffic. This resolution was acted upon by the railroad company as a subscription, and was entered on its minutes, and the promised bonds were disposed of by contract. This court held that the board of supervisors itself had complete authority to make a present subscription, and that the resolution amounted to a subscription, or, at least, to an agreement to subscribe, which, being accepted and acted upon by the railroad company as such, created a contract between the county and the company. In the case before us, no act equivalent to the action of the board of supervisors of Moultrie county was ever done by any person or body of persons, having, at the time of such act, a present power to subscribe for stock or to issue bonds of the town [involved in this case]. The taxpayers had no authority to make a subscription of stock or to issue bonds, or to make any contract to do so; they could only express their desire that it should be done, and that commissioners should be appointed to do it; and when they did express such desire it was continued, as before stated. The commissioners, as we have seen, had no power to act, for no power was given them to act until the railroad was located and completed through [a named village of the county]. It follows that nothing which was done in the present case can be fairly regarded as equivalent to the action of the parties in the case of Moultrie county. The circumstances of the two cases were essentially different."

[1] Town of Solon *v.* Williamsburgh Savings Bank, (1889) 114 N. Y. 122; citing People ex rel. *v.* Mead, 24 N. Y. 114; Kelly *v.* McCormick, 28 N. Y. 318; Board of Education *v.* Fonda, 77 N. Y. 350; San Antonio *v.* Mehaffy, 96 U. S. 312; United States *v.* Linn, 15 Pet. 290. The court additionally said: "At all events, as the commissioners intended to properly and effectually execute the bond, and the omission of the seals was caused by their misunderstanding, mistake or inadvertence, the court of equity may afford the relief requisite to the party justly entitled to the benefit of the instruments and to render them enforce-

these bonds seals had been affixed and were upon them over the places where the scroll opposite the names of the commissioners using them was placed so that the bonds then appeared to have been properly sealed. The defendant purchased them in good faith, and then supposed that the seals were those of the commissioners. The evidence tended to prove that the seals were not affixed by any officer of the railroad company who received them from the commissioners, and that they were not upon them when transferred by the company. It did not appear who were all the intermediate holders of the bonds between the transfer of them by the railroad officers and the purchase by defendant. The trial court found that these seals were affixed by a stranger. Whether or not this worked an alteration of the bonds and its effect upon the rights of the holders was discussed by the Court of Appeals as follows: "If placed there by some one having no interest in the bonds and without any authority, consent or complicity of any person having any interest, the seals would not be treated as effecting any alteration of the bonds. [Citing cases.] If, therefore, this was done by a stranger in the sense of the term applicable in such case, the alteration produced by it would not be effectual to impair the right before existing to enforce the bonds. But, inasmuch as they passed through the hands of other owners before they reached the defendants, it is contended that the finding that it was done by a stranger is not supported, and that the presumption arises that the seals were affixed by some party having an interest in having them put on, and, therefore, explanation is necessary to relieve them from the effect of the alteration. As a general rule, when a material alteration appears to have been made in a written instrument after its execution, evidence is necessary to explain it, and the burden of proof rests upon the party seeking to enforce it to do so to support a recovery upon it. [Citing cases.] The plaintiff's counsel seeks to apply that rule in respect to the burden of proof to this case, and insists that the defendant must bear it. While the burden is with a party seeking to enforce a contract, to relieve it from the effect of any material alteration made in it after its inception, that rule is not necessarily applicable to a defendant in an action brought to have a security held by him canceled upon that ground, when it

able." Citing Wiser *v.* Blachly, 1 *v.* Stebbins, 109 U. S. 341; Cockerell Johns. Ch. 607; Bernards Township *v.* Cholmeley, 1 Russ. & Myl. 418.

appears that such defendant is in no sense chargeable with *mala fides* in that respect. Our attention is called to no authority going to that extent. And the proposition does not seem to commend itself to a court of equity, which is supposed, within recognized bounds, to exercise discretionary powers in such cases."[1]

§ 477. **Proceedings under New York statutes preliminary to issue of bonds.**— A town of New York which had through commissioners appointed for that purpose issued bonds to a certain amount, under the statute authorizing it, in aid of a railroad company, some of which were held by a bank, brought its action in equity against the bank, charging such irregularities, etc., and non-compliance with the statute, as would render the bonds invalid as the town contended, and praying to have the bonds surrendered up and canceled. A judgment was rendered in favor of the defendant, affirmed in General Term and the Court of Appeals when it was considered there affirmed the judgment, holding the bonds to be valid and binding upon the town. The statute under which these bonds were issued provided that "whenever a majority of the taxpayers of any municipal corporation in this state, whose names appear upon the last preceding tax list or assessment roll of said corporation, shall make application to the county judge of the county in which such corporation is situated, by petition, verified by one of the petitioners, setting forth that they are such a majority of taxpayers and represent such a majority of taxable property," etc., the further proceedings may be taken as therein provided for the requisite adjudication and the appointment of commissioners to issue the bonds of the corporation and invest them in the stock or bonds of the railroad company, in view of which the proceeding was taken.[2] The petition addressed to the county judge under this statute in this case contained this statement: "The undersigned, representing a majority of the taxpayers of the town of Solon, in said county of Cortland, whose names appear upon the last preceding tax list or assessment roll of said town," etc. It was signed by persons purporting to be citizens of that town, and upon the petition was the verification by the affidavit of one of

[1] Town of Solon *v.* Williamsburgh Savings Bank, (1889) 114 N. Y. 122, 134, 135; citing on that point McHenry *v.* Hazard, 45 N. Y. 580; Town of Springport *v.* Teutonia Savings Bank, 75 N. Y. 397–408.

[2] N. Y. Laws 1869, chap. 907.

the petitioners, which, among other things, stated that the persons signing said petition are a majority of the taxpayers whose names appear upon the last preceding tax list and assessment roll in said town. It was contended in behalf of the town that the petition failed to set forth that the petitioners were such a majority of the taxpayers by reason of the insertion of the word "representing," which, it was claimed, so far qualified the phrase "a majority of the taxpayers" following it, as to import that such majority did not themselves subscribe the petition, but did it only through the instrumentality of others who were such subscribers, and in the relation of agency represented such taxpayers in thus making the application. The court held adversely upon this contention, and that the petition, as made, was in compliance with the statute and gave jurisdiction to the county judge to entertain the proceeding.[1]

§ 478. **Bonds issued after the passage of an act authorizing a change in their terms.** — The act of 1871, amendatory of the act of 1869, changing the term for which bonds issued by towns in aid of railroads might run, has been held by the New York Court of Appeals to apply to bonds issued after it went into effect, in pursuance of a consent of taxpayers given and adjudicated upon before that time, and, as so construed, that the act was constitutional.[2]

[1] Town of Solon *v.* Williamsburgh Savings Bank, (1889) 114 N. Y. 122.

[2] Brownell *v.* Town of Greenwich, (1889) 114 N. Y. 518, BROWN, J., dissenting. *Arguendo*, VANN, J., for the majority of the court, said: "In Syracuse Savings Bank *v.* Town of Seneca Falls, 86 N. Y. 317, it was held that the act of 1871 applied to proceedings regularly taken prior to its passage. In that case the proceedings were terminated in August, 1870, when the county judge made the adjudication and record, and appointed the commissioners, who delayed action until after May 12, 1871, when they subscribed for stock and issued the bonds. No further consent of the taxpayers was obtained. In Angel *v.* Town of Hume, 17 Hun, 374, the adjudication was made April 22, 1871, and the bonds were issued in February and July, 1872. In both of these cases it was held that the judgment of the county judge, based solely upon the consent of the taxpayers to bond pursuant to the act of 1869, was not nullified or avoided by the amendment of 1871. In neither of those cases had any taxpayer consented to such an issue of bonds, as the amended act gave the commissioners the discretion to issue. In Gould *v.* Town of Sterling, 23 N. Y. 456, the consents were obtained prior to September 29, 1852 (pp. 443, 445), while the bonds were issued in August, 1853 (p. 457). In the meantime an act had been passed authorizing the interest upon the bonds to be made payable on the first

§ 479. Rules as to the taxes collected for payment of bonds issued under New York statutes.— This was an action by a supervisor of a town in New York against the supervisors of the county to recover certain state and county taxes which had been collected of a railroad company which had been aided by the issue of bonds of this town under certain statutes of the state, and which it was claimed had been diverted by the county by the action of its board of supervisors and county treasurer from the use of the town to general county purposes, contrary to certain statutes of the state. The Court of Appeals, upon the question

days of January and July of each year, instead of March first, as was provided by the original bonding act. The only authorities cited to sustain the position that the act of 1871 is unconstitutional are People *v.* Batchellor, 53 N. Y. 128, and Horton *v.* Town of Thompson, 71 N. Y. 513. We do not consider either of them applicable to this case. The only constitutional questions involved in those cases were, in the former, whether the legislature could compel a town to become a stockholder in a railroad corporation by exchanging its bonds for stock without its consent in any way given; and, in the latter, whether the legislature could make a void bond valid after it had actually issued to a person who could not claim as a *bona fide* holder." Returning to the case at bar it was said: "In the case under consideration the consents had been duly given, and an adjudication duly made to that effect, when the amendatory act was passed. There was no want of power, therefore, to issue bonds, as the conditions precedent had all been complied with. The amendment did not extend to matters of jurisdiction, 'but to that which the legislature might have dispensed with the necessity of by the prior statute.' The bonding act would not have conflicted with the Constitution if it had contained no provision as to when the bonds should be made payable, but had left that to the discretion of the commissioners. The provision, therefore, so far as the Constitution is concerned, was immaterial, and could be modified, even retrospectively, at the discretion of the law-making power. In Williams *v.* Town of Duanesburg, 66 N. Y. 137, the court said: 'In this case the legislature could originally have authorized the bonds of the town * * * to be issued under the precise circumstances existing when they were issued; and if the acts of the commissioners have, by subsequent legislation, been ratified, it is equivalent to an original authority to do what has been done. The authorities as to the legislative power to validate, by subsequent legislation, acts done in assumed execution of a statute authority which has not been strictly followed are numerous and decisive.' People *v.* Mitchell, 35 N. Y. 551; Town of Duanesburg *v.* Jenkins, 57 N. Y. 177; People ex rel. Kilmer *v.* McDonald, 69 N. Y. 362; Tifft *v.* City of Buffalo, 82 N. Y. 204; Rogers *v.* Stevens, 86 N. Y. 623. If the legislature has power, after bonds have been issued, to correct irregularities of official action, without affecting the consents of the taxpayers previously given, its power to authorize a change in the form of the bond before it is actually issued, without impairing such consents, cannot well be denied."

of the rights of the town in such case, generally, said: "The right of towns that have issued bonds in aid of railroads, and which are still outstanding, to reclaim taxes collected from the railroad within the town, but diverted to general purposes, is well settled."[1] There was a Statute of Limitations as to such actions, and it appeared as to the claims embraced in this suit for certain years that the board of county supervisors, as organized, at certain dates had passed resolutions referring to the taxes for those years, in which they expressly stipulated and agreed not to interpose the defense of the Statute of Limitations to any sum found due the town on account of the taxes in question. The Court of Appeals held that this stipulation and agreement were within the power of the board of county supervisors.[2] The statutes of New

[1] Woods *v.* Board of Supervisors of Madison County, (1893) 136 N. Y. 403, 405, 406; citing Clark *v.* Sheldon, 106 N. Y. 104; Strough *v.* Supervisors, 119 N. Y. 212; Crowninshield *v.* Supervisors, 124 N. Y. 583; Kilbourne *v.* Supervisors, 62 Hun, 210.

[2] Ibid. The court said: "It is stated as a fact in the case agreed upon that the plaintiff, relying upon the validity of such resolutions, refrained from bringing an action in time for the recovery of the taxes for these years, which, but for such stipulations, he would have done. If the county, through its board of supervisors, can waive the statute like an individual, this would seem to be a writing signed by the party to be charged, and containing a sufficient acknowledgment of the debt and a promise to pay the same within the meaning of the Code. Code, § 395; Chemung Canal Bank *v.* Supervisors, 5 Den. 517; Shapley *v.* Abbott, 42 N. Y. 443; Anderson *v.* Sibley, 28 Hun, 16; Mosher *v.* Hubbard, 13 Johns. 510. Boards of supervisors represent the county in its corporate capacity and have power to bind it to the extent conferred by statute and when any act of such board is challenged as beyond its power, or not binding upon the county, resort must be had to the specific powers enumerated in the statute which such board may exercise. But in such cases the body is not confined to the exercise of the precise act contained in the grant of power, but, from the nature of the case as well as upon settled principles, it possesses and may exercise such incidental powers not expressly enumerated or mentioned in the statute, but which are fairly and reasonably necessary and proper in order to give effect to or carry out the powers expressly conferred. Dillon on Mun. Corp. § 89; Brady *v.* Mayor, etc., 1 Barb. 584; Supervisors *v.* Bowen, 4 Lans. 24. Boards of supervisors are expressly empowered by statute 'to examine, settle and allow all accounts chargeable against the county, and to direct the raising of such sums as may be necessary to defray the same.' It cannot be doubted that the board had power to settle and allow the plaintiff's claim and restore the money which had been appropriated to the benefit of the county at large, instead of investing or using it for the benefit of the town as required by the statute. Nor can it be doubted that in this suit the defendant could have most effectually waived the defense of the Statute of Limitations by honestly, and with-

York, providing for the bonding of towns in aid of railroads, direct the application of taxes assessed upon any railroad in a town toward the redemption of bonds issued by it in the construction of such railroad, and make it the duty of the county treasurer to purchase with such taxes the bonds of the town, or to otherwise invest the same and hold the investment as a sinking fund for the redemption of such bonds. Upon the petition of a taxpayer of a town to compel the county treasurer to apply such taxes in his hands as directed by the statute, the New York Court of Appeals held that a county treasurer, in his relation to such taxes, was not the agent of the county or town, but held them as a trust fund for the purpose expressed in the act, and any action on his part that diverted them from that purpose was illegal. Further, that any taxpayer of the town might apply to the county judge for an order compelling the county treasurer to execute the law in case of his refusal so to do, and it was the duty of the

out collusion, refusing to plead it. Having the power to audit it and settle the claim and to bind the county in that respect, it is difficult to discover any sound reason in law or in morals for the contention that the stipulation in question is not also within the scope of their necessary incidental powers. The board may have been in doubt as to their powers or duty to pay or audit, and by the stipulation it procured time and induced the plaintiff to delay legal proceedings. Under such circumstances, justice requires that the defendant be held bound by the stipulation in the same way as if made between individuals for a like purpose. It was said by CHURCH, Ch. J., in Buffalo *v.* Bettinger, 76 N. Y. 393, that 'a municipal corporation has public and private attributes, and its rights and duties are regulated accordingly. In protecting its property, in collecting its debts, and in general in transacting business of a private character, when not otherwise provided by statute, it may avail itself of the rights and remedies afforded to an individual.' The defendant has capacity to sue and be sued, to audit, settle, pay or compromise claims against it, and this fairly implies power to agree upon terms of payment and to waive by proper agreement the defense of the Statute of Limitations as to claims not barred. This power was exercised in this case for the purpose of relieving the county from actions at law in each year as the time for bringing such suit was about to expire, and we think the bar of the statute is thereby avoided. This result does not disturb the rule, which is conceded, that a county, through its board of supervisors, can exercise only such powers as are expressly conferred by statute, or such incidental powers, not expressly enumerated, as are necessary to carry out the express powers, and, moreover, it is supported by those general principles of equity and justice which are binding upon all corporations as well as upon individuals." As to the rights of a village as to such taxes, see Village of Oneida *v.* Board of Supervisors of Madison County, (1892) 136 N. Y. 269.

county judge to grant the order applied for. Further, in such proceedings, it was no defense that the county treasurer had paid over the fund to an officer of the town, or that the town had had the benefit of it for other town purposes. In this case it appeared that the transactions upon which a claim of the county treasurer, that he had paid over the fund to the town officers, was based, occurred during the pendency of the proceeding of the taxpayer against him before the county judge to compel him to comply with the statute. The Court of Appeals held that his refusal to obey the statute was not only without legal excuse, but was to be regarded as willful; and that he was chargeable with the fund, and also with interest upon it, as the town had been deprived of interest which it would have earned had the law been obeyed.[1] The Court of Appeals has, in another case, held that this statute requiring taxes collected on the assessed valuation of a railroad in a municipality which has issued bonds to aid in the construction of the railroad to be applied by the county treasurer to the purchase of such bonds, or to be invested as a sinking fund for their redemption, is not limited to the bonds originally issued; that where new bonds have been issued to retire and pay off the old ones, they are covered by the provision, as they represent in all respects the same debt.[2] The taxes collected on the assessed valuation of a railroad in a municipality which had issued bonds to aid in the construction of the railroad, instead of being used, as required by the statutes, by the county treasurer to purchase the bonds, or invested by him, having been applied by that officer to the payment of county obligations, the New York Court of Appeals held that the town had an equitable cause of action against the board of supervisors of the county to compel the levying and collection of a tax upon the taxable property of the county for the amount so misappropriated, to be paid to the treasurer and used as required by the statutes. And the fact that the municipality had presented its claim to the board of supervisors and demanded the levying and collection of the tax, and

[1] Clark *v.* Sheldon, (1892) 134 N. Y. 333; s. c., 32 N. E. Rep. 23. See Matter of Clark *v.* Sheldon, (1887) 106 N. Y. 104, in which the court sustained the constitutionality of the statutes under which this proceeding was had. See, also, Strough *v.* Supervisors, 119 N. Y. 212; Crowninshield *v.* Supervisors, 124 N. Y. 583.

[2] Barnum *v.* Board of Supervisors of Sullivan County, (1893) 137 N. Y. 179; s. c., 33 N. E. Rep. 162, affirming 62 Hun, 190.

that the demand had been refused, did not confine the remedy of the claimant to a *certiorari* to review the action of the board, or to a *mandamus* to compel a compliance with the demand. Upon the plea of the Statute of Limitations as a bar it was held that such a cause of action arose when the county treasurer appropriated the money to the payment of county obligations, and the burden was upon the county to show that the money was so misappropriated more than six years before the commencement of the action.[1]

§ 480. **Power of town authorities as to aid bonds under Kansas statutes — for what time they may run.**—As to the authority of a municipal township of Kansas to issue certain kinds of bonds in aid of a railroad, the United States Circuit Court of Appeals for the eighth circuit calls attention to these special provisions of the statute of that state authorizing subscriptions in aid of railroads, to wit: That one which requires a petition by two-fifths of the taxpayers, asking the county commissioners to submit to the township electors a proposition of subscription; such petition to designate the amount of the stock, "the terms of payment," and other conditions of the subscription; the proposition to be accepted by two-thirds of those voting at the election held for that purpose, and the bonds to have coupons attached "as may be required by the terms of said proposition;" the county commissioners to levy a tax "sufficient to pay the interest on such bonds as the same shall become due, and to create a sinking fund sufficient to pay such bonds at maturity," the principal of the bonds to be made payable "at any time that may be fixed in the proposition voted on," not exceeding thirty years. The section after this last declares, among other things, that to the said bond shall be attached coupons for annual installments of "the principal and interest accruing from time to time by the terms of the bonds." The Court of Appeals held that, in view of the prior provisions, the language quoted from the last section did not require that all bonds issued under the act should provide for annual payments on the principal, but merely that if the proposition voted on provided for such annual payments, coupons therefor should be attached, and the

[1] Kilbourne *v.* Board of Supervisors of Sullivan County, (1893) 137 N. Y. 170; s. c., 33 N. E. Rep. 159.

township had authority, by proper proposition, vote, etc., to issue bonds, the whole principal of which should not mature until thirty years.[1]

§ 481. Power of towns in Massachusetts as to aid bonds — their power in the sale of them.—In a rather recent action on contract to recover certain installments of interest on the bonds issued by a town in Massachusetts in aid of railroads, the Supreme Court of Judicature of that state referred generally to the statutes of the state with reference to bonding, etc., and then rendered their opinion as to the power of the towns of that state under those statutes in these words: "We can have no doubt that in this commonwealth the power given to these towns to raise these large or annual sums of money by loans, no conditions or restrictions being imposed, carried with it the power to issue bonds, a method which certainly enabled the towns to seek the best markets. It is, indeed, laid down as a sound doctrine of general application in 1 Dillon Mun. Corp. § 125 that 'express power to borrow money, perhaps in all cases, but especially if conferred to effect objects for which large or unusual sums are required, as, for example, subscriptions to aid railroads and other public improvements, will ordinarily be taken, if there be nothing in the legislation to negative the inference, to include the power (the same as if conferred upon a corporation organized for pecuniary profit) to issue negotiable paper with all the incidents of negotiability.' Many decisions are cited in support of this statement, but the recent decision in Merrill v. Monticello, 138 U. S. 673, is to the contrary. However it may be elsewhere, our decision rests upon the usage and the general course of legislation in this commonwealth." As to the regularity and validity of the bonds, it was said: "It is contended by the defendant that, even if the town had power to borrow money and issue the bonds therefor, the issue was irregular and invalid, because the bonds were delivered directly to the officers of the railroad company in exchange for the stock for which the town had subscribed, instead of being sold for money. The bonds appear to have been taken at par, and there has been no proof or suggestion, and, so far as we are aware, there is no reason to suppose that they would have brought more than par in the market. The

[1] Township of Washington *v.* Coler, (1892) 51 Fed. Rep. 362.

state got them at that rate. If the railroad company was willing to take them at their fair value, it would have been a vain and useless proceeding to require the towns to sell them in the market for cash and pay over the money to the railroad company. This was not necessary."[1]

§ 482. **Power of towns in Mississippi as to aid bonds — for what time they may run.**— A town in Mississippi, under the statute of March 25, 1871, of that state, authorizing the issue of bonds of counties, cities and towns in payment of subscriptions by the municipalities to the capital stock of a railroad company, issued such bonds maturing at from eleven to seventeen years. In an action by a holder of certain of these bonds and coupons thereon past due, in the demurrer to the declaration, it was claimed by the town that the bonds sued on, being payable more than ten years after their execution, were void. The Supreme Court of the United States affirmed the decision of the Circuit Court of the United States sustaining the demurrer to the declaration on this ground.[2]

[1] Commonwealth *v.* Williamstown, (1892) 156 Mass. 70, 73, 74. The court cited to the last statement, Commonwealth *v.* Commissioners of Allegheny, 37 Pa. St. 237, 241; Rogers *v.* Burlington, 3 Wall. 654, 666, 667. The court cited, also, various statutes and these additional cases: Chapin *v.* Vermont & Massachusetts Railroad, 8 Gray, 575; Edwards *v.* Marcy, 2 Allen, 486; Haven *v.* Adams, 4 Allen, 80; White *v.* Vermont & Massachusetts Railroad, 21 How. 575.

[2] Barnum *v.* Okolona, (1893) 148 U. S. 393. Mr. Justice SHIRAS, speaking for the court, declared the law of the case to be as follows: "That municipal corporations have no power to issue bonds in aid of a railroad except by legislative permission; that the legislature, in granting permission to a municipality to issue its bonds in aid of a railroad, may impose such conditions as it may choose; and that such legislative permission does not carry with it authority to execute negotiable bonds except subject to the restrictions and conditions of the enabling act, are propositions so well settled by frequent decisions of this court, that we need not pause to consider them. Sheboygan County *v.* Parker, 3 Wall. 93, 96; Wells *v.* Supervisors, 102 U. S. 625; Claiborne County *v.* Brooks, 111 U. S. 400; Young *v.* Clarendon Township, 132 U. S. 340, 346. Accordingly, if, in the present instance, the legislature of Mississippi, in authorizing the town of Okolona to subscribe for stock in a railroad company and to pay for the same by an issue of bonds, prescribed that such bonds should not extend beyond ten years from the date of issuance, such limitation must be regarded as in the nature of a restriction on the power to issue bonds. Norton *v.* Dyersburg, 127 U. S. 160; Brenham *v.* German American Bank, 144 U. S. 173, 188." There was a contention on behalf of the holder of the bonds that no such limitation was put by the enabling act on bonds issued by towns;

§ 483. **Actions of bona fide holders on such bonds — what they need not show.**— The Supreme Court of the United States has held that an instruction asked in an action by a holder of certain bonds issued by a town in New Jersey and exchanged for bonds of a railroad as authorized by a statute of that state, "that by the issue presented [the town pleaded *non est factum*] by the pleadings in the case, the burden of showing that he was a purchaser for value, or claims title through such a purchaser, was on the plaintiff," was properly refused.[1] Another instruction

that the restriction to a limit of ten years, contained in the fourth section of the act, was applicable only to the case of bonds issued by counties. To this the court said: "It is true that, in the fifth section of the act, which conferred the power on towns and cities to subscribe for railroad stock and pay therefor in bonds, no express provision is found as to the length of time during which the bonds shall run. As, however, the fifth section does provide that the bonds to be given by towns shall be issued 'in the same manner and with the like effect sufficient in amount to meet the total sum of their respective subscriptions for stock, as the boards of supervisors of the different counties are by this act authorized to do,' and that all 'bonds and coupons of interest issued by said mayor and selectmen shall be alike binding upon said towns respectively, in their corporate capacity, as the said bonds so issued by the said boards of supervisors shall be binding upon said counties respectively,' it seems plain that the legislative intent was that the bonds of the towns should be subject to the ten-year limitation contained in the fourth section. This is the fair and obvious import of the language used. The question involves the construction of the statute of Mississippi and has been decided by the Supreme Court of that state in the case of Woodruff *v.* Okolona, 57 Miss. 806, where it was held that bonds issued under that act, having more than ten years to run, were void, and where, in order to reach that conclusion, it was necessary to hold that the limitation of ten years for the running of the bonds, contained in the fourth section, was applicable to bonds issued by towns under the fifth section."

[1] Montelair *v.* Ramsdell, (1882) 107 U. S. 147, 158. The court said: "The pleadings do not, of themselves, impose upon plaintiff the necessity of showing either that he, or any prior holder of the bonds, was a purchaser for value. As holder he is presumed to have acquired them in good faith and for value. Goodman *v.* Simonds, 20 How. 343; Murray *v.* Lardner, 2 Wall. 110; Shaw *v.* Railroad Co., 101 U. S. 557; Swift *v.* Smith, 102 U. S. 442. The plea of *non est factum* did not put in issue the fact that he was the holder. Legislative authority for an issue of bonds being established by reference to the statute, and the bonds reciting that they were issued in pursuance of the statute, the utmost which plaintiff was bound to show to entitle him, *prima facie*, to judgment was the due appointment of the commissioners and the execution by them, in fact, of the bonds. It was not necessary that he should, in the first instance, prove either that he paid value or that the conditions preliminary to the exercise by the commissioners of the authority conferred by statute were, in fact, performed before the

was asked in this case and refused, to wit: "If the evidence satisfies the jury that there were circumstances of fraud or illegality in the inception of the bonds or in the circumstances under which they were issued and disposed of by the commissioners, then the plaintiff cannot recover on the bonds without some proof that he purchased them for value, or gave some consideration for them." The counsel on behalf of the town contended that it was competent under the plea of *non est factum* to prove either fraud or illegality in the inception of the bonds, in order to remove the presumption of *bona fide* ownership for value which arises from the mere possession of the bonds, and thus compel plaintiff to show that *he* paid value for them; consequently the foregoing instruction should have been given. The Supreme Court of the United States held that it was properly refused.[1]

bonds were issued. The one was presumed from the possession of the bonds; and the other was established by the statute authorizing an issue of the bonds, and by proof of the due appointment of the commissioners and their execution of the bonds, with recitals of compliance with the statute. So we have often ruled in numerous cases with which the profession are familiar and which need not be cited." Illustrations of who are not *bona fide* purchasers of bonds of a town, Lansing *v.* Lytle, 38 Fed. Rep. 204. A transferee of such bonds in an action brought against him for their surrender and cancellation has imposed upon him the burden of showing that he or the one under whom he claims was a *bona fide* purchaser. Lytle *v.* Lansing, 147 U. S. 59; citing Stewart *v.* Lansing, 104 U. S. 505.

[1] Montclair *v.* Ramsdell, (1882), 107 U. S. 147. The court said: "[The refusal to give this instruction] was proper for the reason, if there were no other, that it required the jury, if they believed either fraud or illegality in the inception of the bonds to have been established, to find for the township, unless the plaintiff proved that *he* purchased for value or gave some consideration for them. Such is not the law; for if any previous holder of the bonds in suit was a *bona fide* holder for value, the plaintiff, without showing that he had himself paid value, could avail himself of the position of such previous holder. * * *" This question was directly adjudged in Commissioners *v.* Bolles, 94 U. S. 104. One of the issues there was whether the plaintiff was a *bona fide* holder of certain municipal bonds. After stating that the legal presumption was that they were, the court, speaking by Mr. Justice STRONG, said: "But the plaintiffs are not forced to rest upon mere presumption to support their claim to be considered as having the rights of purchasers without notice of any defense. They can call to their aid the fact that their predecessors in ownership were such purchasers. To the rights of those predecessors they have succeeded. Certainly, the railroad company paid for the bonds and coupons by paying an equal amount of their stock, which this county now holds; and nothing in the special facts found shows that the company knew of any irregularity or fraud in their issue." The court proceeded: "And still more; the contractor for building

§ 484. **Bonds absolutely void — effect upon holders.**—The Supreme Court of Illinois has held that where bonds of a municipal corporation are issued without any power or authority in law, as under what purported to be a law, but which was not passed in the constitutional mode, they are absolutely void, no matter in whose hands they may be; but if the legal power or authority to issue them existed, but was defectively or irregularly executed, they are only voidable, and an innocent holder may collect them. Where they are void, no subsequent act or recognition of their validity by the municipal authorities can estop the taxpayers from

the railroad received the bonds from the county in payment for his work, either in whole or in part, after his work had been completed. There is no pretense that he had notice of anything that should have made them doubt their validity. Why was he not a *bona fide* purchaser for value? The law is undoubted that every person succeeding him in the ownership of the bonds is entitled to stand upon his rights." The court in this case then resumed: "When the instruction [here] was asked, the proof was that the bonds had been issued by the commissioners, and exchanged with the railroad company for a like amount of the company's income bonds. That exchange was a substantial compliance with the statute. It was made under a contemporaneous agreement between the commissioners, the railway company and certain trustees, mutually selected, whereby the bonds passed upon the exchange, under the control of those trustees, and were deposited in the Union Trust Company, to be surrendered — ten thousand dollars at a time — only as the work of constructing the railroad progressed, to the company or the contractor on their order. The receipt of the trust company shows that it agreed to deliver them to the contractor or his agents or assigns, on the joint order of the trustees or any two of them, and it was proven that the bonds were delivered to the contractor or upon his order between May 10, 1870, and August 4, 1871. The road was constructed as contemplated, and the income bonds of the company remained in the hands of the commissioners or of some of them. Whether those bonds ultimately proved to be of any value, is of no consequence as between the township and the plaintiff. It thus appears that when the court was asked to give an instruction upon the basis that the plaintiff could not recover, unless it was proven that he paid value for the bonds, it was established beyond question that the bonds had previously passed into the hands, or become pledged for the benefit, of the contractor who built the road. He acquired an interest, or a lien, on the bonds, to secure payment of the amount due him for his work and labor. He, therefore, became a holder for value in the sense that he paid real, in contradistinction from apparent, value, without notice of any fraud or illegality affecting the bonds. Story on Notes, § 195; Railroad Company *v.* National Bank, 102 U. S. 14; Byles on Bills, 117. No evidence was introduced or offered which in any degree impeached his good faith, or proved knowledge on his part that the preliminary conditions prescribed by statute had not been fully performed. The character of the bonds as negotiable securities,

denying their legality.[1] Negotiable bonds which have been issued without statutory authority in payment of a subscription to the stock of a railroad company, which subscription a town, in pursuance of statutory authority, makes, are absolutely void, and no suit can be maintained on them on the theory that they are valid as non-negotiable instruments.[2]

free from defenses which might have been available as between the original parties, was established by their being pledged for the benefit of the contractor. So that, even if there was fraud or illegality in the inception of the bonds (apart from such illegality as would have made them absolutely void by whomsoever held), a defense upon that ground would not have been good against the contractor, and consequently is not available against the plaintiff. The latter, in virtue of the new and independent title derived from or traced to a prior *bona fide* holder for value, could stand upon the rights of such holder." The questions of pleading and rules of evidence in actions on town aid bonds are very fully discussed in Brown *v.* Point Pleasant, 36 W. Va. 290.

[1] Ryan *v.* Lynch, (1873) 68 Ill. 160. As to this distinction, as repeatedly recognized, the court cited Clark *v.* Board of Supervisors of Hancock County, 27 Ill. 308; Johnson *v.* Stark County, 24 Ill. 75; Schuyler County *v.* The People, 25 Ill. 185; Board of Supervisors *v.* Weider, 64 Ill. 427; Marsh *v.* Fulton County, 10 Wall. 683. In a later case (Barnes *v.* Lacon, [1877] 84 Ill. 461) the court adhered to their ruling in Ryan *v.* Lynch, 68 Ill. 160, and as the bonds, in their opinion, were absolutely void, held that the holder could not recover on them. They said: "This rule is well settled in this and other courts. The position of [the plaintiff] is, however, untenable upon another ground. The bonds contain a recital on their face that they are issued in payment of a subscription made by the town of Lacon by virtue of a vote of a majority of the voters at a special election held in said town on the 22d day of December, 1868. This was notice to the purchaser, when he was informed by a recital in the bonds that they were issued in pursuance of a vote of the people at an election held at a special time, and there was no law in existence authorizing the election to be held at that time. As he cannot claim to be ignorant of what the law was, he was bound to take notice of the illegality of the election."

[2] Dodge *v.* City of Memphis, (1892) 51 Fed. Rep. 165; citing Mayor *v.* Ray, 19 Wall. 468; Hitchcock *v.* Galveston, 96 U. S. 350; Little Rock *v.* Merchants' Nat. Bank, 98 U. S. 308; Wall *v.* Monroe Co., 103 U. S. 78; Hill *v.* City of Memphis, 134 U. S. 198; s. c., 10 Sup. Ct. Rep. 562; Merrill *v.* Monticello, 138 U. S. 673; s. c., 11 Sup. Ct. Rep. 441. Referring to these cases, THAYER, J., said: "They show, no doubt, that when a municipal corporation sells bonds which are void, and receives the money, it may be compelled to restore it in an action for money had and received. So, when a municipal corporation is authorized to purchase property for any purpose, or to contract for the erection of public buildings, or for any other public work, and it enters into such authorized contract, but pays for the property acquired or work done in negotiable securities, which it has no express or implied power to issue, it may be compelled to pay for that which it has received in a suit brought for that

§ 485. When a curative act of the legislature will not validate them.—In a case before the Illinois Supreme Court, where it was held that a subscription of a certain sum to the stock of a railroad company, being voted in a town meeting without authority, was void and conferred no power on the town authorities to issue railroad bonds, the effect of a certain act of the legislature, the intention of which was to make the subscription binding upon the town, was fully considered by the court. The question before the court was whether the legislature could create a debt against a town and require the town to assess a tax for its payment. The object of the act being to compel the town to issue bonds for railroad stock independently of its own wishes, as viewed by the court, the act was held to be one violative of the Constitution and of no effect.[1] There was a contention in the case that the legislature might have authorized the town supervisor and town clerk, as the corporate authorities of the town, to subscribe to the stock of the railroad corporation and issue township bonds therefor without a vote of the people, and that the curative act was to be considered as giving them that power, which they had duly exercised. The court held adversely to this contention.[2]

purpose. In no case, however, does it appear that a suit has been sustained on a void bond treating it as non-negotiable and as something entirely different from what the parties intended it should be."

[1] Marshall *v.* Silliman, 61 Ill. 218. The court referred to the provision of the then existing Constitution that "the corporate authorities of counties, school districts, cities, towns and villages may be vested with power to assess and collect taxes for corporate purposes, such taxes to be uniform in respect to persons and property within the jurisdiction of the body imposing the same," and the rulings of the court previously construing this clause in Harward *v.* The St. Clair & Monroe Levee Drainage Co., 51 Ill. 130; People ex rel., etc., *v.* The Mayor of Chicago, 51 Ill. 30; Hessler *v.* Drainage Comrs., 53 Ill. 110, and Lovingston *v.* Wider, 53 Ill. 302, as settling the doctrine that, under that Constitution the legislature could not compel a municipal corporation to incur a debt for merely local purposes against its own wishes.

[2] Marshall *v.* Silliman, (1871) 61 Ill. 218. The court distinguished Town of Keithsburg *v.* Frick, 34 Ill. 420, which was relied upon to support this contention, in these words: "It was said in that case that the legislature might grant that power to the trustees of a town, if it thought proper to do so, without taking a vote of the people. We do not dissent from that position, but it does not aid the appellees in the present case. The town supervisor and clerk who issued the bonds do not represent a township as the board of trustees represent an incorporated town or the common council represent a city. The super-

§ 486. **Effect of curative act of New York.**— The effect of a curative act of the state of New York upon the bonds issued by a town in that state, under its laws, in aid of a railroad, being before the United States Supreme Court, this court, by reason of a judgment rendered in the Court of Appeals of New York that this act, in its main features, was unconstitutional, and this judgment, the town contending, being conclusive upon the Supreme Court, very fully considered the statutes of the state of New York with reference to such municipal aid. After a review of the decisions of the courts of New York pertinent to the question, they held that the subsequent act of the legislature effectually cured the defects in connection with the original issuing of

visor and town clerk are but a part of the corporate authorities. They have no power of taxation nor power of themselves to bind the city in any way. The case of Lovingston *v.* Wider, 53 Ill. 302, may again be cited. We said there that the police commissioners were not the corporate authorities of East St. Louis, as they had not been elected by the people of the city nor appointed in any manner to which the people had given their consent, and, therefore, the legislature could not give them the power of taxation by creating a debt binding upon the city. So of the supervisor and clerk. Though elected by the people, they were not elected for the purpose of creating a debt or imposing a tax, and the legislature could not clothe these two officers, without the consent of the people, with a discretionary power of taxation or of creating a debt, because they are not by themselves the corporate authorities in the sense of the Constitution. But even if these two officers could be recognized as the corporate authorities, they cannot be said to have voluntarily incurred this debt on behalf of the town. The act gave them no discretion. It declares the subscription shall be binding and may be collected. It did not authorize the corporate authorities to subscribe to the stock or not, as they should think proper, but declared that an illegal vote should be a valid subscription, and left to the town authorities only the ministerial function of executing the behest of the legislature. Counsel for appellees claim that this case is like that of Cowgill *v.* Long, 15 Ill. 202. There is, however, a broad distinction. The tax in that case was a valid tax, and when the court say in their opinion that it was improperly voted in July, they evidently mean merely that it was improperly voted in that month for the purpose of collection during the current year. The tax was legally imposed, and the only question decided by the court was that the subsequent act of the legislature legalizing the steps by which the tax was illegally certified to the County Court and placed in the course of collection during that year was so far effectual that the tax could be collected by virtue of the act. The act dealt with a subject entirely under the control of the legislature, namely, the subject of remedy. The question before the court was very different from the ratification of a void tax by retrospective legislation, which the legislature could not of its own power impose prospectively."

these bonds, and that they were valid obligations in the hands of the holder in this case.[1]

§ 487. Township bonds under South Carolina laws made a legal indebtedness by subsequent legislation.— The Supreme Court of South Carolina, by a majority of the court, having held in 1888 that township bonds, issued in aid of rail-

[1] Thompson *v.* Perrine, (1880) 103 U. S. 806. The cases reviewed by the Supreme Court in the opinion rendered by Mr. Justice HARLAN were Bank of Rome *v.* Village of Rome, 18 N. Y. 38; People *v.* Mitchell, 35 N. Y. 551; People *v.* Batchellor, 53 N. Y. 128; Town of Duanesburgh *v.* Jenkins, 57 N. Y. 177; Williams *v.* Town of Duanesburgh, 66 N. Y. 129; Clark *v.* City of Rochester, 13 How. Pr. 204. The court considered Horton *v.* Town of Thompson, 71 N. Y. 513, not binding upon it, and gave reasons why it was not. In Thompson *v.* Perrine, *supra*, as to the rights of the holders, it was said: "It is, therefore, an immaterial circumstance that the recitals in the bonds may have furnished notice that they were issued originally in violation of the statute. That was the very difficulty which the act of 1871 was designed to remove, and, as matter of law, it was removed, if regard be had to the settled doctrines of this court, or to the decisions of the highest court of the state, rendered previously to, and which were unmodified at, the passage of that act. It results that from that moment the bonds, by whomsoever held, whether by the railroad company or by others, became binding obligations upon the town, as much so as if they had originally been sold and their proceeds invested in the stock of the railroad company, as required by the acts of 1868 and 1869. If the rights of those holding the bonds were in any degree affected by the subsequent decision in People *v.* Batchellor, 53 N. Y. 128, the later decision in Town of Duanesburgh *v.* Jenkins, 57 N. Y. 177, restored the law, so far as the courts of New York were concerned, as it undoubtedly was declared to be at the time the act of 1871 was passed. The defendant in error acquired the bonds in suit in 1875, before the decision in Horton *v.* Town of Thompson, 71 N. Y. 513, and when, according to the principles announced in Town of Duanesburgh *v.* Jenkins, and many prior cases in the Court of Appeals, the act of 1871 must have been sustained as a valid exercise of legislative power. He purchased them for value at public auction in the city of New York, without notice of any defense thereto or of the pendency of any suit involving their validity. If the recitals in the bonds gave notice that the acts of 1868 and 1869 forbade their exchange for stock and required them to be sold and their proceeds invested in such stock, the purchaser is also presumed to have known, not only that such exchange had been legalized by the act of 1871, but that the authority of the legislature to pass that act was sustained by the decisions of the highest court of the state, rendered prior to its passage. His rights, therefore, should not be affected by a decision rendered after they accrued, which decision is in conflict with the law as declared not only by this court in numerous cases, but by the highest court of the state, at and before the time he purchased the bonds."

roads to be constructed through those townships, were invalid,[1] the legislature of that state in December, 1888, passed an act to provide for the payment of township bonds issued in aid of railroads in that state.[2] Certain bonds of a county of that state, executed before the passage of this act, had been placed in the hands of a trust company, but before they could be delivered to the parties entitled it was necessary that the engineer of the road should certify as to the completion of the road, and then the chairman and clerk of the board of county commissioners of that county were to affix their signatures to the certificate of the engineer. The engineer had given the certificate required by him, but the county officials above mentioned refused to affix their signatures. The parties entitled to these bonds thereupon petitioned the Supreme Court of the state for a writ of *mandamus* to compel these county officials to affix their signatures to the engineer's certificate, and thus enable these petitioners to have the bonds delivered to them. The Supreme Court dismissed the petition, holding that where a township voted a subscription to a railroad under an unconstitutional statute, and the county commissioners, as the agents of such township, issued bonds in payment therefor, and the county commissioners, assuming to act as such agents, made a contract with a trust company, whereby the trust company took possession of said bonds and agreed to deliver them to a construction company whenever the engineer of the railroad company certified that the railroad was completed through such township, and when this certificate was countersigned by the chairman of the board of county commissioners, attested by the clerk, the subscription, the issue of the bonds and the trust indenture being all unauthorized and void, *mandamus* would not lie after the railroad had been completed to compel such chairman to countersign, and such clerk to attest his signature to the certificate of the chief engineer that the road had been so completed.[3] The Supreme Court of South Carolina, in another peti-

[1] See Floyd *v.* Perrin, 30 S. C., 1; s. c., 8 S. E. Rep. 14. McGowan, J., dissented.

[2] See 20 St. at Large (S. C.), 12.

[3] State ex rel. C. C. & C. R. Co. *v.* Whitesides, (1889) 30 S. C. 579. McGowan, J., said: "I concur, the meaning of the opinion of the court being that there is no necessity for the issue of any new bonds; but 'the debt' fixed upon the several townships by the act of 1888 shall be represented by the bonds heretofore issued, to be paid according to the provisions of the act; and I am authorized to say that such is the view of the other members of the court." See Massachusetts & S. Const. Co. *v.* Cane Creek Tp., (1891)

tion for *mandamus* as to these township bonds, held that *mandamus* would not lie to compel a county treasurer to pay out money on a coupon of a railroad aid bond, when the only constitutional law that recognized such bonds and its coupons as a debt declared that no tax should be levied to pay interest on such debt until the railroad had been completed, and that all taxes theretofore collected for that purpose should be refunded to the taxpayers; and where no tax had been, or could have been, collected since the railroad was completed, the court in this case held that the act of 1888,[1] providing for the payment of township bonds in aid of railroads in that state, was not intended to validate a previous statute which this court had pronounced unconstitutional, nor to legalize acts done thereunder, but to impose upon consenting townships a debt which they had vainly attempted to impose upon themselves under such unconstitutional statute.[2] In a suit upon the bonds in aid of a railroad, issued by

45 Fed. Rep. 336, referring to South Carolina township bonds, holding that where township bonds are declared invalid by the courts, and the legislature afterwards passes an act providing for the payment of such bonds, the debt represented by the bonds is incurred at the date of such act.

[1] See 90 St. at Large (S. C.), 12.

[2] State ex rel. Dickinson *v.* Neely, (1889) 30 S. C. 587; s. c., 9 S. E. Rep. 664. The court sustained the constitutionality of the act of 1888. After calling attention to the distinction between the two classes of power of the legislature, the one which it exercises at its own sovereign will, the other which it delegates to some subordinate agency, to be exercised by such agency at its will, within the prescribed limits, it is said: "Bearing these distinctions in mind, it must be obvious that when this court decided in Floyd *v.* Perrin, 30 S. C. 1, that the act purporting to delegate power to a township to levy a tax for a purpose other than a corporate purpose was unconstitutional, it did not touch the question whether the legislature might not, by the exercise of *its own* power, impose a tax for the same purpose for which it had, without constitutional authority, attempted to delegate the power to certain townships. That decision rested on the ground that as the purpose for which the legislature attempted to delegate to the townships the power of taxation was not a corporate purpose, the act purporting to delegate such power was without constitutional authority. No such question is presented or can arise in this case. The only question here is whether the legislature can, by the original exercise of its own power of taxation, impose a tax on the property within the boundaries of Cherokee township for the purpose of contributing to the construction of a railroad which passes through said township. The proposition that the construction of a railroad is such a public purpose as to warrant the levy of taxes to aid in building it is too well settled by the very decided weight of authority to admit of further discussion, although, if the question were an open one, its correctness might well be disputed. So, too, it seems to be settled by the weight of authority that the legisla-

this township of South Carolina, it was held in the federal court that the statute of that state of December, 1888 (20 Stat. [S. C.] 12), declaring all township bonds theretofore issued in aid of railroads to be a debt of the township, authorizing the levy of a tax to pay it, and providing that the bonds might be used as evidence of the amount and character of such debt, impressed such debt on the township *proprio vigore*, and it was liable therefor, although the act authorizing the issue of the bonds was unconstitutional and the bonds void ; as to the interest, it was held that where an interest coupon covered a period before and after the completion and acceptance of the road, only so much of the interest as was earned after such completion could be recovered under the statute of December, 1888, which provided that no tax should be levied to pay any interest which may have accrued on such bonds prior to completion and acceptance of the road. There was a further ruling that voluntary payments made upon invalid coupons, prior to completion and acceptance of the road, could not be set off against those maturing afterwards.[1]

ture may not only delegate this power of levying taxes to aid in the construction of a railroad to municipal corporations, but may also, by the exercise of its original power of taxation, directly impose such tax upon any territorial division of the state, to aid in the construction of a railroad supposed to be of special advantage to the people residing within such territorial division, provided a majority of those people have signified their assent to the imposition of such a tax. Indeed, some of the authorities hold that the tax may be imposed without the consent of the inhabitants of the territorial division upon which the tax is imposed. But we are not prepared to go to that extent. What is said in the opinion of the chief justice in the case of State *v.* Whitesides, 30 S. C. 579, 584, 585, is not to be regarded as a decision that such a tax may be imposed directly by the legislature without the consent of the people of the particular locality to be affected thereby, but simply as a statement of the fact that some of the authorities go to that extent. Except for governmental purposes proper, we do not think that the legislature has the power to impose a tax upon the people of any particular locality or territorial subdivision of the state without their consent. In this case, however, such consent was given, and that is the avowed basis upon which the act of 1888 rests. It is argued, however, that such consent has only been manifested by an election held without authority of law, and hence should not be regarded. It seems to us that it is not at all material how the assent of the people has been given. All that was necessary was that the legislature should be satisfied that consent had been given, and the terms of the act, especially the preamble, show plainly that they were notified of that fact."

[1] Granniss *v.* Cherokee Township of York County, (1891) 47 Fed. Rep. 427.

§ 488. An Ohio statute as to town aid held unconstitutional.— The Supreme Court of the United States has held that the act of the legislature of Ohio of April 9, 1880, authorizing townships having a population of 3,683, under the census of 1870, "to build railroads and to lease or operate the same," and "to borrow money" as a fund for that purpose, and "to issue bonds therefor in the name of said township," is repugnant to the provisions in the State Constitution, that "the general assembly shall never authorize any county, city, town or township, by vote of its citizens or otherwise, to become a stockholder in any joint-stock company, corporation or association whatever, or to raise money for, or loan its credit to or in aid of, any such company, corporation or association," and the bonds of such a township, issued under the supposed authority of that act, were held to be void.[1] The United States Circuit Court for the northern district of Ohio, upon the case being remanded to the court by the United States Supreme Court, followed the latter and held the act unconstitutional and the bonds void.[2]

§ 489. Miscellaneous rules as to town aid bonds.— The issuing of township bonds to aid in constructing within its limits the depots and side tracks of an existing railroad, has been held to be authorized by the act of Kansas authorizing townships with other municipal corporations "to issue bonds for the purpose of building bridges, aiding in the construction of railroads, water power or other works of internal improvement," etc.[3] Negotiable bonds made by a township in Kansas, under legislative authority, reciting that they were issued "for the purpose of aiding internal improvements in said townships," have been held valid in the hands of a holder for value, notwithstanding they had in fact been issued to aid in the improvement of a water power, and the erection of a water mill owned by private persons.[4] The *bona fide* purchaser of municipal bonds is under no obligation to look beyond the action of the persons or tribunal authorized by law to determine the result of an election held for the purpose of ascertaining whether the municipality should issue its bonds in

[1] Pleasant Township *v.* Ætna Life Insurance Co., (1891) 138 U. S. 67; s. c., 11 Sup. Ct. Rep. 215.

[2] Ætna Life Ins. Co. *v.* Pleasant Township, (1893) 53 Fed. Rep. 214.

[3] Rock Creek Township *v.* Strong, 96 U. S. 271.

[4] Guernsey *v.* Burlington Township, 4 Dill. 372.

aid of an object authorized by law, as such action is conclusive.[1] A township in Michigan had voted railroad aid bonds with a condition precedent to the delivery of the bonds that the road should not only be in running order, but an equivalent amount of the company's stock should be delivered to the township treasurer. Before this was done a new township was set off from the one which voted the bonds. The Supreme Court of that state held that until the exchange of bonds for stock was made there were no contract relations with the railroad company, and that even if the bonds had been valid, the new township would not be bound by a judgment against the old township for the amount of the bonds.[2] Attaching conditions to the signatures to a petition for the issue of railroad aid bonds will not necessarily vitiate the petition.[3]

[1] Rock Creek Township *v.* Strong, 96 U. S. 271.

[2] Beeman *v.* Black, 49 Mich. 598.

[3] Town of Andes *v.* Ely, 15 Sup. Ct. Rep. 954. A case holding a town estopped to set up the defense of *ultra vires* as to bonds which were regular upon their face and purported to have been issued in accordance with the act of the legislature authorizing them, Town of Brewton *v.* Spira, (Ala.) 17 So. Rep. 606. In Linn *v.* Chambersburgh Borough, (1894) 160 Pa. St. 511, a bill in equity to restrain the borough from undertaking the erection of an electrical plant, on the ground that the borough indebtedness would be increased beyond the constitutional limit, it was held that the burden was on the plaintiff to prove that the indebtedness would be necessarily increased to an amount exceeding the legal limit. Railroad aid bonds held not invalidated in the hands of a *bona fide* holder in Union Bank *v.* Board of Comrs. of Town of Oxford, (N. C.) 21 S. E. Rep. 410. As to the power of the legislature under a constitutional provision that the legislature may permit municipal corporations to assess and collect taxes for corporate purposes only, to authorize such corporations to issue bonds in aid of railroad companies, see Town of Darlington *v.* Atlantic Trust Co., 68 Fed. Rep. 849. See, also, Atlantic Trust Co. of New York *v.* Town of Darlington, 63 Fed. Rep. 76. The Supreme Court of South Carolina has held a provision in an act of the legislature allowing female adults, owning $100 worth of taxable property within the corporate limits of the town, to vote at an election to be held in the town upon the question of issuing town bonds in aid of a railroad to be valid as within the power of the legislature. Woodley *v.* Town Council of Clio, (S. C. 1895) 22 S. E. Rep. 410, following Wilson *v.* City Council, 39 S. C. 397; s. c., 17 S. E. Rep. 835; approved in 40 S. C. 290; s. c., 18 S. E. Rep. 792.

CHAPTER XXV.

BONDS AND COUPONS — PRIVATE COPORATIONS.

§ 490. Bonds of private corporations, generally.
491. Meeting of stockholders to authorize the issuance of bonds — when legally held.
492. Interest on bonds — what rate, etc.
493. When principal becomes due.
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501. Holders of income bonds — rules as to an accounting with them.
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503. Actions on coupons — rules governing.
504. Guaranty of bonds of one corporation by another — rules.
505. Lease of a bonded railroad — when lessee is not bound on the bonds.

§ 490. **Bonds of private corporations, generally.**— Private corporations, in the conduct of their business, are vested with power to give, as obligations, their bonds as a means of borrowing money for their legitimate business purposes, or in payment of debts incurred in carrying out the purposes of their creation, unless there be some restriction upon them by statute.[1] These bonds are known, generally, as coupon bonds, because attached

[1] Peoria & Springfield R. R. Co. *v.* Thompson, 103 Ill. 187; Brown *v.* Maryland, 62 Md. 439; McLane *v.* Placerville & Sacramento Valley R. R. Co., 66 Cal. 606; Mead *v.* New York, Housatonic & Northern R. R. Co., 45 Conn. 199; Kelly *v.* Trustees, etc., 58 Ala. 489; Da Ponte *v.* Northern Pac. R. R. Co., 21 Blatchf. 534; Coe *v.* Columbus, Piqua & Ind. R. R. Co., 10 Ohio St. 372; Commonwealth *v.* Smith, 10 Allen (Mass.), 448; Craven *v.* Atlantic & North Carolina R. R. Co., 77 N. C. 289; Miller *v.* New York & Erie R. R. Co., 18 How. Pr. 374; Dana *v.* Bank of the United States, 5 Watts. & Serg. 223; McMasters *v.* Reed, 1 Grant's Cas. 36; Hubbard *v.* New York & Harlem R. R. Co., 36 Barb. 286. As to the power and right to issue income bonds, see Garrett *v.* May, 19 Md. 177.

and connected with them are usually interest coupons, for the terms at which the interest on the bonds is to become due; mortgage bonds, or bonds secured by mortgage or trust deed of the property of the corporation to a trustee for the bondholders; income bonds, secured by a mortgage of the income of the corporation, and debenture bonds. These bonds are usually made payable to bearer, and are negotiable, passing generally by delivery.[1] The statements in a certificate accompanying a bond that it is secured by a mortgage must be construed with the bond and mortgage as a part of the same security.[2] Bonds of a corporation chartered to build a canal that contained recitals that they should have preference over all debts to be thereafter contracted, and that, in default of payment of interest, the holder of the bonds might enter into the possession of the tolls, water rates and other incomes of the company, and might apply for the appointment of a receiver, have been held by the United States Supreme Court in effect to constitute a mortgage, and the holders of the bonds entitled to the relief usually granted in case of a mortgage.[3] The effect of the provisions of the Civil Code of California upon the bonds and mortgage of a railroad company was considered in a case, and it was held that, in a bond payable at a fixed date, a provision that the obligor may, at its option, redeem the

[1] Ide *v.* Passumpsic & Connecticut Rivers R. R. Co., 32 Vt. 297; Edwards *v.* Marcy, 2 Allen, 486; White *v.* Vermont & Massachusetts R. R. Co., 21 How. 575; Morris Canal & Bkg. Co. *v.* Fisher, 9 N. J. Eq. 667; Carr *v.* Le Fevre, 27 Pa. St. 413; Chapin *v.* Vermont & Massachusetts R. R. Co., 8 Gray, 575; Langston *v.* South Carolina R. R. Co., 2 S. C. 248; Hubbard *v.* New York & Harlem R. R. Co., 36 Barb. 286; Brainerd *v.* New York & Harlem R. R. Co., 25 N. Y. 496; s. c., 10 Bosw. 332; Dinsmore *v.* Duncan, 57 N. Y. 573; Welch *v.* Sage, 47 N. Y. 143; Hodges *v.* Shuler, 22 N. Y. 114; Virginia *v.* Chesapeake & Ohio Canal Co., 32 Md. 501; Junction R. R. Co. *v.* Cleneay, 13 Ind. 161. As to formalities of bonds, see Hendee *v.* Pinkerton, 14 Allen, 381; Allen *v.* Sullivan R. R. Co., 32 N. H. 446; Royal Bank of Liverpool *v.* Grand Junction R. R. & Depot Co., 100 Mass. 444; Chilton *v.* People, 66 Ill. 501; Bates *v.* Boston & N. Y. Central R. R. Co., 10 Allen, 251. When a *bona fide* purchaser of such bonds has a right to presume the requirements of a statute as to the execution of bonds have been complied with, see Connecticut Mut. Life Ins. Co. *v.* Cleveland, Columbus & Cincinnati R. R. Co., 41 Barb. 9. That the board of directors and president of the corporation have power without the concurrence of the stockholders to authorize the issue of bonds and mortgage, see Hodder *v.* Kentucky & Great Eastern Ry. Co., 7 Fed. Rep. 793.

[2] Benjamin *v.* Elmira, Jefferson & Canandaigua R. R. Co., 49 Barb. 441.

[3] White Water Valley Canal Co. *v.* Vallette, 21 How. 414.

same before maturity at any date when the semi-annual interest is due, did not render the bond so uncertain, as to time or amount, as to deprive it of its negotiable quality under the provisions of the Civil Code of California, sections 3087–3089, 3091, 3093. The constitutional provision of California that the stock and bonded indebtedness of corporations shall not be "increased" without the consent of the person holding the larger amount of the stock, does not apply to the first creation of bonded indebtedness.[1] It was found in an Illinois case, an action to annul certain bonds as *ultra vires* the railway corporation to issue, that the president and general manager of the corporation, without any authority, used the bonds which came into his hands to pay debts of other corporations which were under his control, and "not in any way about the construction, equipment or operation" of the railway corporation, and that the bonds were acquired by the holders with full knowledge that they had been misapplied in the manner they were. These findings the Supreme Court of the state held to exclude the hypothesis that the corporation, the debts of which were paid with the bonds, might have agreed to construct or equip the road in part, and were sufficient to support the decree declaring the bonds null and void as against the railway corporation.[2] A traffic contract had been made by a railway corporation, which had executed certain bonds payable in thirty years, with another railway corporation, agreeing that it should retain the former's share of the earnings and pay them over semi-annually to a trustee, to be applied to the ultimate redemption of the bonds. The contract, by its terms, was to continue for thirty years, "or for so long a time as will be sufficient to provide a fund large enough to redeem all of said bonds." The agreement was indorsed on the bonds. This agreement was held in a federal court not to give the corporation issuing the bonds the right to pay off the bonds as soon as a fund sufficient for that purpose had accrued and before the expiration of the thirty years.[3] A construction company, employed by a railroad corporation to build its track under an agreement, was to have issued to it by the railway corporation bonds of the latter to a certain amount

[1] Union Loan & Trust Co. *v.* Southern California Motor Road Co., (1892) 51 Fed. Rep. 840.

[2] City of Chicago *v.* Cameron, 120 Ill. 447; s. c., 11 N. E. Rep. 899.

[3] Chicago & Iowa R. Co. *v.* Pyne, 30 Fed. Rep. 86.

per mile of track, in installments, as sections of the work should be completed. The bonds of the railroad corporation, by a subsequent agreement, were delivered in advance of the building of the track, the construction company agreeing to take care of and pay all interest accruing before the road was in condition for traffic, and the railway corporation agreed to reimburse the construction company for all interest paid, not properly chargeable to it, out of the first earnings of the road. A federal court held that the proper construction of the contract was that the construction company was only bound to pay interest on so many of the bonds as it received and used to which it was not entitled under the construction contract.[1] That it was known to the executive committee of the directors of a corporation that a purchaser of its mortgage bonds purchased them under a belief that the proceeds were to be used for a particular purpose, has been held in New York not sufficient to bind the corporation to a trust limiting the use of the proceeds of the bonds sold.[2] The charter of a consolidated corporation recited the uses to which money to be derived from the sale of its bonds was to be applied, and a trust agreement was entered into in accordance with the terms of the charter. The bonds of the corporation were sold under a prospectus pointing out a source of inquiry as to the charter and trust. The prospectus, however, misstated the purpose for which the proceeds of the bonds were to be used. A federal court held that the trustees were not liable to the bondholders for having used the proceeds in accordance with the trust agreement, and not in the manner set out in the prospectus. It was further held that the company, having sold its bonds by an agent who issued a prospectus stating to what uses the money was to be applied, did not establish a fiduciary relation between the bondholder and the company, and the bondholder could not pursue the money received for the bonds as a trust fund where the company had parted with it to another for a different use, the latter having obtained title as between himself and the company.[3] It appeared in a case that a firm engaged in negotiating bonds for the company negotiated a large number of them, of which fact it did not notify the company. Afterwards, the firm purchased them back and loaned the

[1] Foster *v.* Mansfield, C. & L. M. Ry. Co., 36 Fed. Rep. 627.

[2] Ives *v.* Smith, 3 N. Y. Supp. 645.

[3] Bischoffsheim *v.* Brown, 34 Fed. Rep. 156; Banque Franco-Egyptienne *v.* Brown, 34 Fed. Rep. 162.

company's trustees a sum less than it had received from the sale of the bonds to be used for a certain purpose, pretending to hold the bonds as a collateral for the loan. The court held that this firm could not, on the trustees' applying the money to the uses of their trust, though different from those agreed upon with the firm, follow the property into the hands of those to whom it had been paid, without paying the trustees the money which had been received from the sale of the bonds, the trustees having an equitable title to such money.[1] It was provided in a mortgage executed by a railroad company that certain bonds secured by it remaining in the hands of the trustee should not be issued unless with the assent of a majority in amount of the outstanding preferred stock, and that if any part of such bonds should be used for the construction of branches or extensions, the same should only be countersigned and delivered by the trustee at a rate not exceeding $20,000 per mile of new construction, and upon the certificate of the engineer of the mortgagor that sections of not less than ten miles had been completed, ready for operation. This provision of the mortgage was held in a federal court not to authorize the trustee to refuse to issue them except for continuous sections of ten miles each; that the company was entitled to have the bonds issued for every ten miles of new construction completed and ready for operation, whether in branches, each shorter than ten miles, or in the excess over ten-mile sections.[2] Mortgage bondholders of a corporation, who subscribed to the debenture bonds of the corporation, agreed to pay specified portions of their subscription as called for, they to receive therefor the debenture bonds bearing interest, etc. This undertaking on the part of the bondholders was held by the Supreme Court of Judicature of Massachusetts to be in effect an agreement to loan the corporation money, and not analagous to an unpaid subscription to capital stock; and, therefore, on that theory the creditors of the corporation could not maintain a bill to have the subscriptions to the debenture bonds applied to their claims. It was further held that the fact that the debenture bonds were issued to enable the corporation to complete its railroad did not create any trust in favor of creditors whose claims were for supplies furnished in the

[1] Ibid.

[2] Denver & Rio Grande R. Co. *v.* United States Trust Co., 41 Fed. Rep. 720, an action to compel the trustee to countersign and issue the bonds.

construction of the road; that this contract between the corporation and its bondholders who subscribed for these debenture bonds being executory on both sides, and not assignable by either party, was not within Public Statutes of Massachusetts, chapter 151, section 2, clause 11, giving creditors a remedy in equity to reach and apply "any property, right, title or interest, legal or equitable," belonging to a debtor.[1] Bonds secured by mortgage having been issued by an organization assuming to act as a corporation, and put in circulation, the holders of the stock of such corporation cannot defeat the bonds and mortgages by alleging that the corporation was not duly incorporated.[2] The fact that the road was constructed for less than the amount of the bonds a railroad company may have issued to pay for its construction, will not invalidate such bonds where the contract for construction has been fairly made and carried out and called for that amount.[3] The bonds in this case were issued under the mortgage securing them by a railroad company which had leased its railroad for a

[1] Pettibone *v.* Toledo, C. & St. Louis R. Co., 148 Mass. 411; s. c., 19 N. E. Rep. 337. As to overissue of bonds, see Stephens *v.* Benton, 1 Duv. (Ky.) 112. As to what form of contract would pass title to railroad bonds under particular circumstances, see American Loan & Trust Co. *v.* Toledo, C. & S. Ry. Co., (1890) 47 Fed. Rep. 343. Under what conditions the fact that bonds were issued by a corporation when insolvent does not render them void, see Cochran *v.* Anglo-American Dry Dock & Warehouse Co., 69 Hun, 168; s. c., 23 N. Y. Supp. 404. Bonds of a manufacturing corporation delivered to a bank to secure indebtedness held valid, though the trust company to which the mortgage to secure the bonds was to be given, had not signed them before the delivery to the bank, notwithstanding the bonds provided they would not be valid until signed by the trust company in Gunther *v.* Mayer, 138 N. Y. 654; s. c., 34 N. E. Rep. 513. When a stockholder of a corporation is estopped to contest the validity of its bonds, see Zabriskie *v.* Cleveland, Columbus & Cincinnati R. R. Co., 23 How. 381. When bonds of a corporation hypothecated as a collateral will be held void, see Pfister *v.* Milwaukee Electric Ry. Co., 83 Wis. 86; s. c., 53 N. W. Rep. 27.

[2] Phinizy *v.* Augusta & K. R. Co., 62 Fed. Rep. 678.

[3] Farmers' Loan & Trust Co. *v.* Rockaway Valley R. Co., 69 Fed. Rep. 9. As to when bonds issued by a railroad corporation in excess of the amount of cash paid on its capital stock, or to pay for constructing a road other than the one specified in its articles of incorporation, to be used as a branch line, and secured by a mortgage containing on its face what amounts to a promise by the corporation to observe the law governing the making of such bonds and mortgages, will be held valid in the hands of innocent purchasers, and void in the hands of others, see Baker *v.* Guarantee Trust & Safe Deposit Co., (N. J. Eq.) 31 Atl. Rep. 174.

term of fifty years to a railroad company owning a majority of the shares of its capital stock, the lease providing that the lessee should furnish the necessary rolling stock and equipment for the operation of the railroad, and should receive out of the revenues of the road a reasonable compensation for the use of such rolling stock and equipment. The bonds were five per cent bonds and to mature in forty years. They were taken by the lessee company at ninety per cent of their face value in consideration of a large debt due the lessee company, rolling stock sold to the mortgagor company, and stocks and bonds of other corporations owning roads connecting with and forming feeders of the railroad of the latter company sold to it by the lessee company. Minority stockholders filed a bill praying that these bonds and the mortgage securing them should be declared null and void and decreed to be delivered up for cancellation. The main allegation of the bill was that the transaction consummated by the issuing of the bonds and mortgage in question was a fraudulent scheme concocted for the benefit of the corporation holding the majority of the stock to enable it to raise money for its own purposes, and carried out to the prejudice of the other stockholders of the company, by means of the domination and control which the former company had over the management of the affairs of the latter. The Supreme Court held that these minority stockholders could not complain of an issue of mortgage bonds to a holder of the majority of the stock when such issue was made by the corporation without fraud, for an adequate consideration and with great benefit to the corporation, though the issuance was procured by the majority stockholder for use to raise money for itself and was actually so used.[16]

§ 491. Meeting of stockholders to authorize the issuance of bonds — when legally held.—In this foreclosure suit it was objected to the validity of the bonds that the meeting called to increase the bonded indebtedness of the railroad company was not held within the state as required by the statute of Alabama, which provides that a stockholders' meeting for such a purpose must be held in the state, that the call must state the time, place and object of the meeting, and that a report of the meeting must be filed with the secretary of state. It appeared that notice was

[16] Gloninger *v.* Pittsburgh & Connellsville R. R. Co., (1890) 139 Pa. St. 13; s. c., 21 Atl. Rep. 211; 27 W. N. C. 497.

given to the stockholders of the railroad company of a meeting to be held at a place in the state of Alabama on April 20, 1887, to increase the bonded indebtedness of the company, and prior to that date every stockholder consented in writing to the increase. On March 24, 1887, the board of directors held a meeting in the state, at which the call of the stockholders' meeting and the written consent of all the stockholders were recited, and the issuance of the bonds were authorized; and subsequently a report of the directors' meeting, reciting the stockholders' consent, was filed with the secretary of state. The court held that there was a sufficient compliance with the law of Alabama as to such meetings, and the issue of the bonds was legally authorized.[1]

§ 492. **Interest on bonds — what rate, etc.**—The railroad bonds upon which this bondholders' suit was based, were issued by a South Carolina railroad company, and the interest was made payable in London. One of the questions before the United States Supreme Court was what rate of interest the principal of these bonds bore. It was held by the court that the contract being made in one place and the performance of the contract to be in another, both as to the interest and the principal, and the interest before maturity being payable according to the legal rate in the place of performance, the presumption was, in the absence of attendant circumstances to show the contrary, that the principal of these bonds bore interest after maturity at the same rate — the rate fixed by the laws of England and not the rate fixed by the laws of South Carolina.[2] There was a covenant in coupon

[1] Coe *v.* East & West R. Co. of Ala., (1892) 52 Fed. Rep. 531; Grant *v.* East & West R. Co. of Ala., (1892) 52 Fed. Rep. 531. In Hodder *v.* Kentucky & Great Eastern Ry. Co., 7 Fed. Rep. 793, it was held that the mortgage of the property of the Kentucky corporation to secure the bonds could be legally acknowledged by its president in the state of Ohio. Bonds and mortgages of corporations organized under Illinois laws have been held not to be invalid merely because executed out of the state. Hervey *v.* Ill. Mid. Ry. Co., 28 Fed. Rep. 169.

[2] Coghlan *v.* South Carolina R. Co., (1891) 142 U. S. 101; s. c., 12 Sup. Ct. Rep. 150. Mr. Justice HARLAN, for the court, after a reference to the authorities upon the subject of such contracts generally, as to this particular one said: "What law, then, did the parties have in view as determining the legal consequences resulting from the non-performance of the contract between them? Presumptively, the law of England, where the contract was to be entirely performed. The bonds and coupons were to be presented and paid there and not elsewhere. They were to be paid in pounds sterling at a designated house

bonds, issued by a railroad corporation, that a sinking fund, sufficient to pay a certain amount of the bonds and accrued interest, should be provided on November fifteenth in each year until the whole amount of the bonds should be paid; that the numbers of the bonds to be paid in each year should be determined by drawing lots, and that the principal of the bonds so drawn should "be payable at the option of the holders, * * * upon the surrender of the bonds drawn, with all the coupons thereto belonging, and after the said 15th day of November the interest upon the bonds should cease." A court of New York has held the option of the holders of the bonds so drawn under this covenant applied only to their right to retain possession of the bonds, and that interest on such bonds ceased on the November fifteenth for which they were drawn, whether surrendered by the holders or not.[1]

§ 493. **When principal becomes due.**— The mortgage bonds in this foreclosure suit contained the provision that "it is hereby expressly agreed by said company, with each and every holder of this bond, that, in case of the non-payment of any interest coupon hereto attached, if such default shall continue for six months after maturity and demand of payment, the principal of this bond shall become immediately due." The United States Circuit Court of Appeals for the fifth circuit held that the six months was not in addition to days of grace, but was to run

in London. The fair inference is that the railroad company negotiated the bonds abroad and made them payable in that city in order to facilitate a sale of them to foreign buyers. Every circumstance connected with the contract tends to show that the parties intended that all questions in respect to performance or the legal consequences of a failure to perform were to be determined by the law of the place, and the only place, where the obligation to make payment could be discharged, and where the breach of that obligation would occur if payment was not made at the appointed time and place. In this view of the contract the rate of interest, after the maturity of the obligations, was not determinable by the law of South Carolina. This is abundantly established by the authorities." See Scudder *v.* Union National Bank, 91 U. S. 406, 412; Scotland County *v.* Hill, 132 U. S. 107, 116; Hall *v.* Cordell, (1891) 142 U. S. 116 (upon a bill of exchange drawn in Missouri payable in Illinois). As to interest and the sale of bonds below par, see Craven *v.* Atlantic & North Carolina R. R. Co., 77 N. C. 289; McGregor *v.* Covington & Lexington R. R. Co., 1 Disney, 509; Morrison *v.* Eaton & H. R. R. Co., 14 Ind. 110; Traders' National Bank *v.* Manufacturing Co., 96 N. C. 298; Coe *v.* Columbus, Piqua & Indiana R. R. Co., 10 Ohio St. 372; Junction R. R. Co. *v.* Bank of Ashland, 12 Wall. 226.

[1] Henry *v.* Syracuse, G. & C. R. Co., 5 N. Y. Supp. 437.

from the date on which the coupons were expressed to be due, and the default having continued in the case two days more than the six months, the bondholders were entitled to declare the principal immediately due. Further, the recitation in the bond as quoted above restricted the provision for the maturity of the bonds for non-payment of interest to the particular bond or bonds on which interest was not paid. Also, an acceptance of interest after the default had continued longer than six months was a waiver of the right to declare the bonds matured. It appearing in the foreclosure suit that the interest was paid on some of the bonds, it became necessary to take an account of the bonds which were properly declared to have matured; and the Court of Appeals held the decree adjudging the bonds to be due to be erroneous and reversed it on that ground.[1]

§ 494. **Bonds — when "issued" under Wisconsin statutes.** — In a bill in a Court of Chancery brought by a judgment creditor, his execution having been returned *nulla bona*, for the appointment of a receiver and an injunction against a water company and certain purchasers at foreclosure of its property and franchises who had received from this water company bonds to the amount of $100,000 as collateral for $40,000, money advanced, and had afterwards contracted to advance $27,000 more, a part of which had been advanced, the question of the validity of these bonds was before the United States Circuit Court for the eastern district of Wisconsin. The water company had issued bonds to the amount of $125,000, depositing the $25,000 with a trust company under deed of trust. It was held by the court that the bonds, although pledged as collateral and not sold, were "issued" within the meaning of the Revised Statutes of Wisconsin, section 1753, which declares void any bonds issued by a corporation, except for money actually received, equal to seventy-five per cent of their par value; and that these bonds were not enforceable in the hands of the pledgee.[2]

§ 495. **When a mortgage trustee should countersign bonds.** — The trustee of a railroad mortgage, a trust company, was sued to compel it to countersign and deliver certain mortgage bonds

[1] Alabama & Georgia Mfg. Co. *v.* Robinson, (1893) 56 Fed. Rep. 690; citing Railroad Co. *v.* Fosdick, 106 U. S. 47; s. c., 1 Sup. Ct. Rep. 10.

[2] National Foundry & Pipe Works *v.* Oconto Water Co., (1892) 52 Fed. Rep. 29, in which a receiver was appointed, an injunction granted and the bonds,

to the complainant in the suit. The trustee had refused, relying for justification of its refusal upon a provision in the mortgage that certain bonds secured by it remaining in the hands of the trustee should not be issued unless with the assent of a majority in amount of the outstanding preferred stock; and that, in the event any part of such bonds should be used for the purpose of constructing branches or extensions, the same should only be countersigned and delivered by the trustee at a rate not exceeding $20,000 per mile of new construction, and upon the certificate of the engineer of the mortgagor that sections of not less than ten miles had been completed ready for operation. WALLACE, J., of the United States Circuit Court for the southern district of New York, held that the mortgage did not authorize the trustee to refuse to issue them except for continuous sections of ten miles each, but that the company was entitled to the bonds for every ten miles of new construction completed and ready for operation, whether in branches each shorter than ten miles or in excess over ten-mile sections.[1]

§ 496. Pledge of bonds by a corporation — rights of pledgee, etc. — The statute of Michigan as to railroads provides that "all companies organized under this act shall have power, from time to time, to borrow such sums of money as may be necessary for completing, finishing, or operating their road, or any part thereof, or for paying any indebtedness necessarily incurred for completing, finishing, or operating their road, or any part thereof, and to issue and dispose of their bonds or obligations for any amount necessarily borrowed for such purpose, and for such sums and for such rate of interest, not exceeding ten per cent, as they may deem advisable, and to mortgage their corporate property and franchises, and income thereof, or any part thereof, to secure the payment of any debt contracted, * * * and said company may sell their bonds or obligations either within or with-

by order of the court, were to be delivered into the hands of its officers until further order of the court.

[1] Denver & Rio Grande R. Co. *v.* United States Trust Co., (1890) 41 Fed. Rep. 720. The court said: "The object of the clause manifestly is to protect the bondholders against the creation of mortgage indebtedness for new construction not secured by actually completed new lines and against the contingency that bonds might be issued ostensibly to pay for new construction and be used for some object from which the bondholders would derive no benefit. It is framed so as to enable the trustee to know that the bonds to be issued represent completed lines ready for operation and not merely projected new construction."

out the state, and at such place and prices as they may deem proper." There was in this case a resolution in stockholders' meeting of a company in that state directing its managing body "to borrow such sums of money as they may think necessary for completing, equipping and operating its road, * * * and to issue and dispose of the bonds of the company for any amount borrowed for such purpose, for such sums and for such rates of interest, not exceeding seven per cent, as they may deem advisable, and to mortgage the corporate property and franchises, and the income thereof, to secure the same, and to sell such bonds on the best terms they may be able to obtain for the same." They borrowed money from a national bank and pledged some of their bonds issued under this resolution for the payment of the sums borrowed. The United States Circuit Court of Appeals for the sixth circuit held that, under the Michigan statute and the resolution of the stockholders, the corporation was empowered and authorized to pledge its bonds for the money borrowed.[1] It appearing upon foreclosure proceedings that the bonds of a street car company, issued pursuant to a vote of the stockholders "for the purpose of extending and constructing" the road, purchasing rolling stock and equipment, and paying "for labor done and to be done in the construction" and operation of the road, were never sold to procure funds for these purposes, but that, after ineffectual attempts to sell them, were pledged by the president and vice-president of the mortgagor to secure antecedent indebt-

[1] Farmers' Loan & Trust Co. *v.* Toledo & S. H. R. Co., (1893) 54 Fed. Rep. 759. JACKSON, Circuit Judge, said: "Under the New York statute, from which [the Michigan statute] is evidently taken, it is settled that under authority to borrow money and 'to issue and dispose of bonds' in connection therewith, there is a right to pledge such securities as collateral for the sums borrowed. Duncomb *v.* Railroad Co., 84 N. Y. 190. So in Beecher *v.* Mill Co., 45 Mich. 103; s. c., 7 N. W. Rep. 695, where bonds of a corporation were issued on the understanding that they were to be sold for cash, but were in fact pledged to a creditor as collateral to corporate notes held by him, it seems to have been held by the court that the objection that such disposition of the bonds was unlawful could only be taken by the corporation or its stockholders; that it was not open to strangers or even to a purchaser of the equity of redemption at execution. Without going into a review of the decisions, we are of opinion that the weight of modern authority, as well as sound principle, establishes the general rule that, in respect to negotiable securities, authority to sell carries with it authority to pledge. Platt *v.* Railroad Co., 99 U. S. 48; and Leo *v.* Railroad Co., 17 Fed. Rep. 275."

edness of the company, which to a large extent was due to other companies of which also they were officers and directors, it was held by the United States Circuit Court for the southern district of California that the pledge was without authority, and in fraud of the rights of the stockholders.[1] The lower court in the foreclosure suit decreed in favor of a bank which had loaned the railroad corporation a large sum of money on bonds of the corporation pledged to it as collateral, the amount loaned with interest, which was not as much as the face of the bonds represented. The United States Court of Appeals for the sixth circuit held that this was erroneous, and that the holder of these bonds was entitled to have a decree for the whole amount due upon them.[2] A railroad company, incorporated

[1] Farmers' Loan & Trust Co. *v.* San Diego St. Car Co., (1891) 45 Fed. Rep. 518, in which case, as in the opinion of the court none of the bonds in question ever were legally issued, or ever became valid outstanding obligations of the defendant corporation, the bill for foreclosure of mortgage was held not to be well pled. It was said by the court: "Aside from the want of legal power already referred to, a court of equity will not permit the directors of a corporation, who are not only trustees for the stockholders of the corporation, but for its creditors as well, to thus dispose of the corporate property to themselves, or for their individual benefit. However in fact intended, equity treats such transfer as fraudulent, because it operates as a fraud upon the *cestui que trustent.* Koehler *v.* Black River, etc., Co., 2 Black, 717." See, also, upon the general subject, Richardson's Exrs. *v.* Green, 133 U. S. 30; s. c., 10 Sup. Ct. Rep. 280. In California, it is provided by statute that "neither a trustee, nor any of his agents, may take part in any transaction concerning the trust in which he, or any one for whom he acts as agent, has an interest, present or contingent, adverse to that of his beneficiary," with certain enumerated exceptions not applicable to the present case. Civil Code Cal. § 2230. And section 2234 of the same Code declares that every violation of the provisions, among others, of section 2230, "is a fraud against the beneficiaries of the trust." These Code provisions have been held applicable to the directors of corporations in their trust relations by the Supreme Court of the State. Graves *v.* Mining Co., 81 Cal. 303; s. c., 22 Pac. Rep. 665.

[2] Farmers' Loan & Trust Co. *v.* Toledo & S. H. R. Co., (1893) 54 Fed. Rep. 759. JACKSON, Circuit Judge, said: "The sale and purchase of these bonds by the bank under and within the terms of the railroad company's note and pledge of the collateral were not *per se* void. It was at most only voidable, at the instance and upon reasonable objection on the part of the corporation or its stockholders. Third parties or strangers have no right to question or challenge the bank's title to the bonds on the ground either of inadequacy of the price paid for the same, or for the reason that it occupied such a *quasi* trust relation to the pledgee as to disqualify it from purchasing at a sale made for its own benefit. The securities having been regularly issued and hypothecated as

under the laws of Virginia, executed a first mortgage upon its road, to secure bonds to the amount of $15,000 per mile. The greater portion of these bonds passed into the hands of purchasers. Afterwards, desiring to build an extension of its road, the stockholders authorized a second mortgage to the same trustees as in the first mortgage, to secure bonds to the amount of $25,000 per mile of its road. The resolutions as to this second mortgage, and all the proceedings preliminary to the execution of this second mortgage, showed the intention to be to take up the bonds issued under the first mortgage by an exchange of second mortgage bonds, or raising of money on the latter and paying off the former. The railroad company, foreseeing that it might not be able to exchange the general mortgage bonds for the first mortgage bonds, made this provision, that "until all bonds which have been and may hereafter be issued under the security of the first mortgage * * * shall come into the hands of the trustee of this mortgage under this provision," [the provision for exchange] "and the trustees of this mortgage shall determine the advisability of the satisfaction and release of the said first mortgage * * * all such first mortgage bonds which shall come into the hands of the trustees, under this provision, shall be held by the trustees uncanceled for the security and benefit of the holders of the bonds secured thereby; * * * " Fifteen days after the general mortgage was executed, bonds, to the amount authorized under the first mortgage, not already issued, were, in pursuance of the prescribed terms, duly issued by the railroad company and delivered by its treasurer to the trust company as trustee on the first mortgage. These bonds under the general mortgage were sold principally to a syndicate under the terms of a prospectus which virtually pledged these bonds issued under the first mortgage as a collateral for the security of the bondholders under the general mortgage. The general mortgage was afterwards fore-

collateral for a debt the company was authorized to contract, and thereafter lawfully sold under the terms of the pledge, upon proper notice, even the maker of the paper could not impeach the purchaser's title thereto, and the right to recover the amount thereof, without setting up and establishing fraud or breach of trust causing injury. Such an objection by way of impeachment of the purchaser's title to the pledged security is confined to the corporation or its stockholders. [This intervener's] relation to the railroad company was not such as entitled him to question the bank's title to the bonds, or complainant's right, as the legal representative of the bondholders, to foreclose for the full amount thereof."

closed. In the final decree the court below held that the bondholders under the general mortgage were entitled to share in the security of the first mortgage to the extent of $1,560,000, the amount of the first mortgage bonds deposited with the trustee as collateral security for the payment of the general mortgage bonds. The majority of the Supreme Court of Virginia affirmed the decree of the lower court, holding that in placing these bonds as security for the general mortgage bonds the company violated no rights of the first mortgage bondholders; that as to these bonds both sets of bondholders stood upon the same footing; that there was no overissue; that the failure of the trustees to certify these particular bonds, as directed, did not affect their validity.[1]

§ 497. **Validity of bonds — as affected by statutory or constitutional provisions.**— The Code of Alabama requires subscriptions to railroad stocks, which are payable in labor or property, to be taken at their money value, which must be stated in the subscription list. In this case it appeared that a railroad company adopted a resolution to sell all its property to another company for $750,000, one-half in stock and one-half in bonds of the purchaser, and subsequently entered a subscription for $375,000 of stock "to be paid for in the railroad property" of the seller, "of the value of the said sum of three hundred and seventy-five thousand dollars." The United States Circuit Court of Appeals for the fifth circuit held that, reading the subscription in connection with the resolution, as it must be, its language was not conclusive that the value of the entire property was not over $375,000, so as to render void the issue of $375,000 in bonds under the constitutional provision forbidding overcapitalization. They declared this further rule, that, under the constitutional provision of that state forbidding corporations to issue stock or bonds except for money, labor or property actually received, and the before-mentioned Code provision as to subscriptions payable in money, labor or property, railroad property sold by one company to another and paid for by an issue of stock, as in this case, may be valued according to its net earning power, and the cost of building it *de novo*, and that it was immaterial that the seller originally acquired it for much less than its actual value.[2] In

[1] Atwood *v.* Shenandoah Valley R. R. Co., (1889) 85 Va. 966.

[2] Grant *v.* East & West R. Co. of Alabama, (1893) 54 Fed. Rep. 569.

this case it appeared that certain stockholders and directors of a railroad company, owning a controlling interest in the company, having the best interests of the company in view, and with the concurrence of all the other stockholders, made a contract on behalf of the company with a construction company for the building of a portion of the road to be paid for in bonds to the extent of $10,000 per mile, and the same amount in stock of the railroad

There was a contention in this case that the taking of the property at double the price which was considered its real value, payable in equal amounts of stock and bonds of said company, was illegal under the Alabama laws, and by absorbing into said bonds the full real value of the property secured on the subscription, worked a fraud on the rights of subsequent creditors, for whose protection that stock of the company and its proceeds constituted a trust fund independent of any state, organic, or statute law. The court held adversely to this contention. McCormick, Circuit Judge, speaking for the court, said: "It has long been the settled doctrine of the United States courts that the capital stock of an insolvent corporation is a trust fund for the payment of its debts; that the law implies a promise by the original subscribers of stock who do not pay for it in money or other property to pay for the same when called upon by the creditors; and that a contract between themselves and the corporation that the stock shall be treated as fully paid and non-assessable, or otherwise limiting their liability therefor, is void as against creditors. Sawyer *v.* Hoag, 17 Wall. 610; Upton *v.* Tribilcock, 91 U. S. 45; Sanger *v.* Upton, 91 U. S. 56; Webster *v.* Upton, 91 U. S. 65; Chubb *v.* Upton, 95 U. S. 665; Pulman *v.* Upton, 96 U. S. 328; Graham *v.* Railroad Co., 102 U. S. 148–161; Hawkins *v.* Glenn, 131 U. S. 319; s. c., 9 Sup. Ct. Rep. 739. And the trust arising in favor of creditors by subscriptions to the stock of a corporation cannot be defeated by a stipulated payment of subscription, nor by any device short of an actual payment in good faith. Camden *v.* Stuart, 144 U. S. 104; s. c., 12 Sup. Ct. Rep. 585. The well-settled doctrine of the general law relating to subscriptions to the stock of corporations, as announced by the United States Supreme Court in the cases above cited, has been embodied in the Constitutions and Codes of many of the states; and issues of stocks and bonds, under constitutional and statutory provisions substantially similar to those in Alabama, have been sustained when they have been disposed of by a corporation after its organization for the best price that could be obtained, though for less than their face value. Railroad Co. *v.* Thompson, 103 Ill. 187; Railroad Co. *v.* Dow, 120 U. S. 287; s. c., 7 Sup. Ct. Rep. 482; Handley *v.* Stutz, 139 U. S. 417; s. c., 11 Sup. Ct. Rep. 530; Clark *v.* Bever, 139 U. S. 96; s. c., 11 Sup. Ct. Rep. 468; Fogg *v.* Blair, 139 U. S. 118; s. c., 11 Sup. Ct. Rep. 476. When the charter of a corporation or the general law under which it is created authorizes the capital stock to be paid for in property, and the shareholders honestly and in good faith pay for their subscriptions in property instead of money, there is an end of trust in favor of anybody, and third parties, even subsequent creditors, have no ground of complaint, although a gross and obvious overvaluation of such property would be strong evidence of fraud in an action by a cred-

company. The United States Circuit Court for the northern district of Alabama held that as the contract appeared to be fair, under the circumstances, and involved no fraudulent overvaluation of the work, the bonds and stock issued in terms of the contract were not void under the provision of the Constitution of Alabama that "no corporation shall issue stock except for money, labor done, or money or property actually received, and all fictitious increase of stock or indebtedness shall be void."[1] A

itor to enforce personal liability. Coit *v.* Gold Amalgamating Co., 119 U. S. 343; s. c., 7 Sup. Ct. Rep. 231."

[1] Coe *v.* East & West. R. Co. of Ala., (1892), 52 Fed. Rep. 531. PARDEE, Circuit Judge, said: "A provision in the Constitution of Arkansas, almost identical with that of the state of Alabama, has been construed by the Supreme Court of the United States not to prevent the carrying out of an agreement by which the bondholders of a railroad stipulated that the road should be bought upon foreclosure by trustees, who should convey it to a new company composed of bondholders, who should receive mortgage bonds of the new company in exchange for their old bonds, and full paid-up stock subject to the mortgage debt, without any payment of money. The court said: 'But appellant disputes its liability upon the bonds given for the balance upon the theory that they were prohibited from issuing them by the * * * Constitution of Arkansas. * * * That section provides that 'no private corporation shall issue stock or bonds except for money or property actually received or labor done, and all fictitious increase of stock or indebtedness shall be void.' In support of this view our attention is called to the fact admitted by the demurrer, that the full value of the property rights and privileges conveyed to appellant did not exceed $1,300,000, the amount at which the capital stock was fixed; and consequently, it is argued, the $2,600,000 of bonds were issued without any consideration received in money, property or labor, and represented only a fictitious indebtedness. In other words, appellant's vendors were fully compensated for their interests by taking to themselves its entire stock. We do not concur in this view of the case. It does not, we think, rest upon a sound interpretation of the State Constitution. The prohibition against the issuing of stock or bonds, except for money or property, actually received, or labor done, and against the fictitious increase of stock or indebtedness, was intended to protect stockholders against spoliation, and to guard the public against securities that were absolutely worthless. One of the mischiefs sought to be remedied is the flooding of the market with stock and bonds that do not represent anything whatever of substantial value. In reference to a provision in the Constitution of Illinois, adopted in 1870, containing a prohibition as to railroad corporations similar to that imposed by the Arkansas Constitution upon all private corporations, the Supreme Court of the former state in Railroad Co. *v.* Thompson, 103 Ill. 187–201, said: 'The latter part of the clause of the Constitution in question which declares that 'all stocks, dividends and other fictitious increase of the capital stock or indebtedness of such corporation shall be void,' we think clearly points out the chief object

Minnesota railroad company entered into a contract with parties to construct a portion of its road. By the terms of that contract a certain amount of the company's first mortgage bonds, guaranteed by another corporation, a mining company located on the company's railroad, and a certain amount of shares of its stock, were to be placed in the hands of a trustee, to be delivered to the contractor when the road was completed. The right of the company to issue these bonds and the stock and use it in this way was questioned in an action by one claiming to be a stockholder of the company to restrain the company from this act, as an *ultra vires* act on its part, it being claimed that it was in violation of the Minnesota statute, prohibiting any railroad company or officer thereof from selling or disposing of shares of its capital stock, or issuing certificates therefor, unless such shares shall have been fully paid, or issuing any stock or bonds, except for money, labor or property received and applied for the purpose for which the corporation was created. It was held by the court that this statute did not forbid the issue of first mortgage bonds and full-paid stock by the company in payment for the construction of the road, if the amount did not unreasonably exceed the value actually received.[1] The statute of New York, providing that no

which the constitutional convention sought to accomplish in adopting it, and to this we must look in a large degree for a solution of the language which precedes it. The object was doubtless to prevent reckless and unscrupulous speculators, under the guise of pretense of building a railroad, or of accomplishing some other legitimate corporate purpose, from fraudulently issuing and putting upon the market bonds or stock that do not, and are not intended to, represent money or property of any kind, either in possession or expectancy, the stock or bonds in such case being entirely fictitious.'" Railroad Co. *v.* Dow, 120 U. S. 287–297; s. c., 7 Sup. Ct. Rep. 482.

[1] Brown *v.* Duluth, M. & N. Ry. Co., (1893) 53 Fed. Rep. 889. NELSON, D. J., said: "This statute was not intended to prevent or interfere with the usual method of raising money to build railroads, or for any legitimate corporate purpose. It is not to be construed as obstructive to the extent of restricting and hampering corporations in their internal management, and embarrass them in procuring means to carry out the legitimate purposes of the corporation; and, unless it appears that under the guise of building its road, bonds and stock of the defendant company are to be issued and put upon the market fraudulently that do not and are not intended to represent money and property, this corporation is not prohibited from entering into a real transaction based upon a present consideration, and having reference to legitimate corporate purposes. Beach on Corp. 909, and authorities there cited. Such a transaction is not a scheme or device to evade the statute. It may be that an amount of corporate bonds and stock turned over by a corporation is so much in excess of the expenditures

corporation shall issue bonds, "except for money, labor done, or property actually received for the use and lawful purposes of such corporation," has been held to prohibit an issue of bonds by the corporation to pay scrip dividends.[1]

§ 498. Validity of bonds as affected by the manner of sale and character of purchasers.— The validity of the bonds of this railroad company received by certain of its stockholders and directors by purchase from a construction company, to which they were issued by the railroad company in payment for the construction of its road upon a contract of so much in bonds and so much in stock per mile, was sustained in a foreclosure suit by the holders of consolidated first mortgage bonds, purchased by them from those to whom they were issued and those bonds for construction taken up by the company. The complainants sought to invalidate the bonds held outside of themselves as being based upon an improper contract for the construction of the road.[2]

to be made by the recipients of the same that a court would hold that the statute prohibited such a transaction; but if the purpose of the corporation in issuing bonds and stock is to build its road and no unreasonable amount is issued beyond the value actually received or provided for, the statute in my opinion does not apply." Citing Railroad Co. *v.* Dow, 120 U. S. 298; s. c., 7 Sup. Ct. Rep. 482.

[1] Merz *v.* Interior Conduit & Insulation Co., (1895) 34 N. Y. Supp. 215. Bonds of a corporation held not a fictitious indebtedness prohibited by the Constitution of Texas, in North Side Ry. Co. *v.* Worthington, (Tex. Civ. App.) 27 S. W. Rep. 746.

[2] Coe *v.* East & West R. Co. of Ala., (1892) 52 Fed. Rep. 531. It was said by the court: "Certainly, if the contract inured to the benefit of the railroad company, and was the best available method for securing the construction of the road, and there was no palpable overvaluation of the work performed and moneys advanced, nor undervaluation of the stocks and bonds received in payment, and it resulted in no injury to any person in interest at the time, it should not be set aside on technicalities, but only in case of palpable intended violation of law. The case of Van Cott *v.* Van Brunt, 82 N. Y. 535, is directly in point: 'The right of the officers of a railroad corporation to enter into an agreement to build its road and pay for the construction of the same in stocks and bonds cannot be seriously questioned, and contracts of this description are frequently made for such a purpose.' In Angell & Ames on Corporations (§ 590a) it is laid down: 'An agreement is often made by railroads to pay the persons building them a certain proportion of the contract price in stock. Under such a contract the contractor is entitled to the proportion in stock at its current market value at the time payment should have been made. And if the stock depreciate so that it has no market value, the amount agreed to be paid in stock must be paid in money.' See Hart *v.* Lauman, 29 Barb. 410; Moore *v.* Rail-

These same stockholders and directors, retaining control of the railroad company, failed to collect interest on the first bonds of the company held by them, and advanced to the company money for repairs made necessary by an unusual flood, and for improvements until the floating debt due them amounted to more than $300,000. A meeting of stockholders authorized the issue of debenture bonds of the railroad company, not exceeding $500,000,

road Co., 12 Barb. 156; Porter *v.* Railroad Co., 32 Me. 539. If a contract can be made to pay in part for building a portion of the road, it may also be made to pay for the whole thereof in like manner, and there is no valid ground for claiming that, where the contractor is entitled to stock at its market value, he would be liable for the difference between the market value and the par value thereof. There is no evidence in the record before us to establish affirmatively that the value of the work done and materials furnished was less than the fair and just value of the stock, or that the road built or equipped was worth less than said stock. In fact the testimony shows that the amount expended exceeded the actual value of the stock and bonds which were received in consideration of the same. The evidence also establishes that the stock never had any market value whatever. It is true that some of the bonds were disposed of at fifty and sixty-five cents upon the dollar and less, and in some instances by throwing in stock to the same amount and one-half more, and in one instance taken at par in part payment of a debt, but they were intrinsically valueless, and after a while were sold for only a nominal sum, until at last no one outside of the company would take either the bonds or stock at any real price. The arrangement for the building of the road was made after full deliberation and consultation, with the knowledge and approval of all the directors and stockholders. It was assented to as the only means furnished, and the only offer which could be obtained from any one to insure the construction of the railroad. It was the best thing that could be done under the circumstances, was entirely satisfactory, and made most clearly without any intention to defraud the company or its creditors and in perfect good faith. It is difficult to see how creditors could be defrauded when all the property which the company ever had remained in its possession and under its control. * * * It is claimed that the defendant, as president, director and trustee, having wrongfully appropriated the stock to himself without paying for it, takes all the obligations of a subscriber. This depends upon the question whether the transfer of the stock to the defendant and the application of the same was wrongful. It was done, as we have seen, with the full approval of the stockholders, and in fact was a necessity, and, without the contract entered into, no portion of the road could have been built.. If the defendant had realized a sum beyond the amount actually expended, there might have been perhaps some ground for claiming that the arrangement should inure to and for the benefit of the company. As, however, this was not the fact, and no special advantage accrued to the defendant from the contract, and as there is no proof of any fraud, it is not apparent that there was any wrongful appropriation of the stocks and bonds or that the stocks and bonds were diverted from their legitimate

for the purpose of paying the floating debt, to be secured by a second mortgage. A resolution of the directors had previously determined that these debenture bonds, when issued, should not be disposed of at less than sixty-five per cent of their face value. The court held as to these bonds that the purchase by the holders of the floating debt of the whole amount of bonds authorized, by

use. The mere fact that the defendant held a certificate of the stock which was transferred to him did not make him liable, as it was to all intents and purposes paid-up stock." This case has received some adverse criticism (2 Mor. Priv. Corp. § 826; Cook Stocks & S. § 47, note 5; Jackson *v.* Tracr, 64 Iowa, 483; s. c., 20 N. W. Rep. 764), but it has been cited with approval and its doctrines have been reaffirmed by the court of last resort in the state of New York in the case of Barr *v.* Railroad Co., 125 N. Y. 263; s. c., 26 N. E. Rep. 145, where it is said: "The respondent has questioned the legality or validity of the issue of shares upon which plaintiffs base their right to sue. I do not think it is in a position to raise that question, and for several manifest reasons. All of the stock and bonds were issued in payment for the construction of the railroad, and were taken by a syndicate of persons who assumed the contract for the work. It is true that that syndicate was made up of members of the board of directors, but as the members of the syndicate were practically the company, and composed the whole number of stockholders, there was no one to object, and the manner in which they chose to divide up their interests in the proprietorship of the corporation, and to represent them in shares, concerned only themselves. No principle of law forbade the company agreeing to pay for the construction of its railroad in the way or in the amount it did. Van Cott *v.* Van Brunt, 82 N. Y. 535. If the company's directors were interested in the work and profits of construction, and evaded a direct contract through the form or device of an intermediary contractor, that was a matter for the company or for its stockholders to take hold of. But the stockholders and the members of the syndicate were the same persons, and, however wrong the transaction might be if other persons were concerned, here no injury was effected to any one interested in the corporation. And, however illegal the transaction, there was no person apparently to complain of it. As the stock was issued as a part of the consideration for construction, it cannot be said that it was taken without value given, and the mode of its apportionment or division concerned only those interested in the contract through which it was received as payment. We may concede that the contract was voidable as a scheme concocted by the directors for sharing in the profits of construction, but the difficulty is that the members of the corporation were assenting to it. There was, however, no fraud practiced upon the company. Practically, the promoters of the corporation in this way placed a valuation upon the corporate properties and franchises which the contribution and expenditure of their money created, and the fact that they were created for an expenditure less than the par value of the aggregate issues of capital stock and bonds does not affect the question at all."

the terms of which they paid for them in this floating indebtedness and the balance in cash, was valid.[1] Certain bonds of a railroad company had been placed in the hands of a trust company to be by said trust company, upon the completion of work of construction of an extension of the railroad by a construction company, delivered over to the latter, on certain certificates of the completion of the extension. When the extension was practically completed the bonds were issued on certificates to the construction company, but the trust company retained them to secure prior advances to the construction company. In the foreclosure suit upon these bonds, an intervening judgment creditor, who had constructed a part of this extension under a contract with the construction company, but had brought his action against the railroad company upon which his judgment was recovered, after the failure of the construction company, set up a claim to these bonds so retained by the trust company. The court held that he had no claim to those bonds to subject them to the satisfaction of his judgment, but the court recognized his judgment as a valid judgment against the railroad company, but inferior as a lien to that of the bondholders under the first consolidated mortgage which was being foreclosed.[2] A contract for the lease of a railroad belonging to an iron company was entered into by a railroad company represented by certain stockholders and directors, they being also stockholders and directors of the iron company, which contract was in good faith and in the form of a resolution by the directors of the railroad company, the payment for the lease to be in stocks and bonds of the railroad company and of a subscription by the iron company to be paid in property — a lease of its railroad, and the contract was ratified by a unanimous vote of all the stockholders of the railroad company. The validity of the bonds issued to the iron company in terms of this contract was questioned in this foreclosure suit. It was held by the United States Circuit Court that the contract was, at least, only voidable, and as no fraud or intentional overvaluation appeared, and the consideration was as nearly adequate as could be expected

[1] Coe *v.* East & West R. Co. of Ala., (1892) 52 Fed. Rep. 531. When a purchaser of bonds is put upon inquiry in regard to the regularity or validity of their issue by the low price at which they are offered, see Riggs *v.* Pennsylvania & New England R. R. Co., 16 Fed. Rep. 804.

[2] Coe *v.* East & West R. Co. of Ala., (1892) 52 Fed. Rep. 531; Grant *v.* East & West R. Co. of Ala. (Schley, Intervener), (1892) 52 Fed. Rep. 531.

under the circumstances, the bonds issued to the iron company were valid.[1]

§ 499. **Reorganization — surrender of old bonds and stock for new bonds — rules.**—A bondholder in this case it appeared had declined to surrender and exchange his mortgage bonds pursuant to a reorganization agreement which he refused to accept in a suit to collect the mortgage bonds according to the terms of the original mortgage, while all of the bonds except his were surrendered and exchanged. The federal court in the district where this suit was brought had substantially confirmed the reorganization; the trustee of the bondholders was a party defendant to the suit and fairly represented the rights of all. The interest representing ninety-nine per cent of the bondholders demanded the judgment. The rights of the non-conforming bondholders were fully recognized in the decree of the court by providing that the company should execute an indemnity bond conditioned for the payment of the bonds of those dissenting as to the judgment, and that this bondholder might recover under the decree all he was entitled to. There was a cross-bill filed by the companies to compel this bondholder, who brought the suit, to surrender his bonds and receive in lieu thereof new bonds according to the reorganization agreement. The United States Circuit Court for the southern district of New York held that the decree in the original suit properly protected his interests; that he must surrender his old bonds and accept the new ones as provided for in the agreement, but that he was entitled to the same security afforded the majority bondholders. The cross-complainants, the railroad companies, having taken the position throughout the suit that the bondholder suing could at any time surrender his bonds and receive new ones in lieu thereof under the original decree, and their counsel in their brief having offered to deliver the bonds and cash upon such surrender, it was further held that the cross-complainants were not in a position to insist that the bondholder suing had by his misconduct forfeited his rights to interest.[2] The decree entered in a bill to foreclose a mortgage upon the property of a railroad company in this case authorized such bondholders as should become purchasers to pay their bids in bonds.

[1] Coe *v.* East & West R. Co. of Ala., (1892) 52 Fed. Rep. 531.

[2] Pollitz *v.* Farmers' Loan & Trust Co., (1892) 53 Fed. Rep. 210.

The representative of certain bondholders purchased the property and a master was appointed to report distribution and the form of the conveyances. The master reported that the purchase by the representative above mentioned was on behalf of certain bondholders named, not including the one who brought this action, and of such others as might wish to join in the purchase and pay their proportions of the purchase money and expenses, and that the property was bought to sell again in such manner as three-fourths of the bondholders should direct. The form of deed to the purchaser reported by the master recited that it was in trust for all the bondholders. Afterwards, as directed by three-fourths of the bondholders, the representative of the bondholders conveyed the property to a railroad company, organized by the purchasing bondholders to succeed the former company, "free and discharged from all and every trust whatsoever." The act incorporating this new company recited that the company was composed of persons named and "all others who held mortgage bonds," but the preamble set out the deed to the representative of the bondholders "in trust for all the bondholders who participated in the said purchase," and that it was desirable "to reimburse the said bondholders for their expenditure of money and labor." The plaintiff in this case, as surviving partner of a firm, afterwards discovering among the firm's assets a bond of the old company, which, by its terms, was convertible into stock, brought assumpsit against the corporation formed by the purchasing bondholders to recover for their refusal to exchange stock in the new company for the bond, claiming that the representative of the bondholders took as trustee for all the bondholders of the old company, and that the conveyance to the new company was really with the agreement that the latter company assumed the duties of the representative of the bondholders as such trustee, and that, therefore, the new company was bound to make the exchange which he demanded. The Supreme Court of Pennsylvania held that it was clear, from a consideration of the foreclosure decree, the deeds to and from the representative of the bondholders, the master's report and the act incorporating the new company, that the plaintiff had merely an option to participate in the new venture by coming in within a reasonable time and sharing in the expenses and risk; that the representative's duty, notwithstanding general expressions in the deeds and the

act of incorporation, was to distribute stock to such bondholders as participated in the original purchase or subsequently exercised their option to come in, and the last chance to exercise this option was when the deed was made to the new company clear of all trusts.[1] The United States Supreme Court has given a full consideration to the effect of the constitutional provision of the state of Arkansas that "no private corporation shall issue stock or bonds except for money or property actually received or labor done, and all fictitious increase of stock or indebtedness shall be void." They held that the provision did not prevent the carrying out of an agreement between mortgage bondholders of an embarrassed railroad company in that state by which it was agreed that trustees should buy in the mortgaged property on foreclosure and convey it to a new company which should issue new mortgage bonds to pay the expenses of the sale, and other new mortgage bonds to be taken by the bondholders in lieu of their old bonds and full paid-up stock, subject to the mortgage debt, to be delivered to and held by the bondholders without any payment of money; and, further, the bonds issued under such an agreement were not subject to the provisions of the statutes of that state respecting the legal rate of interest for certain classes of railroad securities.[2]

§ 500. Bondholders — when bona fide holders, and when not — the rights of such. — A *bona fide* purchaser, before maturity, of coupon bonds of a railroad company payable to bearer, takes them freed from any equities that might have been set up against the original holder; and the burden of proof is on him who assails the *bona fides* of such purchase.[3] A *bona fide* holder of negotiable bonds of a corporation is not subject to the general doctrine of *lis pendens;* and this applies even if the bonds were purchased during the pendency of a suit in which the issue of the bonds was finally declared invalid.[4] Bonds which

[1] Landis *v.* West Pennsylvania R. R. Co., (1890) 133 Pa. St. 579. This action was brought thirty years after the sale of the property.

[2] Memphis & Little Rock Railroad *v.* Dow, (1887) 120 U. S. 287.

[3] Kneeland *v.* Lawrence, (1891) 140 U. S. 209, in which the holder was not held to be a *bona fide* purchaser. See Murray *v.* Lardner, 2 Wall. 110, 121, and cases there cited.

[4] Farmers' Loan & Trust Co. *v.* Toledo & S. H. R. Co., (1893) 54 Fed. Rep. 759; citing Lexington *v.* Butler, 14 Wall. 283; Warren County *v.* Marcy, 97 U. S. 96; Douglass *v.* Pike County, 101 U. S. 687; 2 Beach Priv. Corp. § 666.

may have been issued to a contractor who had in course of trade passed title to the bonds to a purchaser in good faith, the latter's right to recover on the bonds is not open to any defenses on the part of the corporation which they may have had against the contractor in connection with the performance of his contract.[1] The purchaser of the bonds of the corporation from its president and one of its directors, inquired of the vice-president, secretary and attorney as to their validity, and was informed by each that the bonds were regularly issued and sold, and were valid. The books of the corporation showed that the bonds were authorized to be sold for $35,000; that the name of the director from whom the purchase was made was entered as the purchaser, and that he was credited with that sum of money. The purchaser from the director was held to be an innocent purchaser, and the corporation was held to be estopped to deny the validity of the bonds, as against him. The corporation which, with the knowledge and consent of all its stockholders, had sold certain of its bonds to its directors for less than par, but for their full actual value, was also held estopped from questioning the validity of the sale of bonds, either as against the directors or their assignees.[2] An objection was urged in this case that the sale of the amount disposed of of general mortgage bonds was negotiated by a banking house, who were the financial agents of the railroad company, and the bonds were purchased or subscribed for by this banking firm, or by members thereof, standing in a fiduciary relation to the railroad company, which rendered the whole transaction invalid, and, therefore, rendered this deposit of the 1,560 bonds as collateral also invalid. The Supreme Court of Virginia held that the principles controlling fiduciary relations had no application; that the transaction was merely a lending of money on one side and a borrowing on the other.[3] The holder of the first

[1] McElrath *v.* Pittsburg & Steubenville R. R. Co., 55 Pa. St. 189.

[2] Union Loan & Trust Co. *v.* Southern California Motor Road Co., (1892) 51 Fed. Rep. 840.

[3] Atwood *v.* Shenandoah Valley R. R. Co., (1889) 85 Va. 966. The court said: "In Hotel Co. *v.* Wade, 97 U. S. 13, it was said: But where stockholders sanction a contract under which directors loan money to the corporation, and its bonds, secured by mortgage, are given, if the money is properly applied, the corporation is estopped from setting up that the bonds and mortgage are void by reason of the trust relations which directors sustained to it. Here the railroad company not only obtained the loan on the terms dictated by it, but received the cash and actually expended it in the construction of the extension of its

mortgage bonds of this railroad company contracted with brokers to sell them all their bonds; they transferred to the brokers a portion of the bonds, and together with the brokers fraudulently procured the listing of the bonds on the New York Exchange. The complainants in the auxiliary suit for foreclosure of this mortgage, who had purchased some of these bonds, which had been pledged to them as loans made to the brokers, claimed that they were entitled to priority upon their bonds to those held by the bondholders in the main suit, on account of fraud practiced upon them. The court held that complainants in the auxiliary bill, who loaned money to the brokers on these bonds as security, relying either on the standing and representations of the brokers, or on quotations made in the New York Stock Exchange, and produced by fictitious manipulations of the brokers, and not on the false representations as to the earnings of the company, etc., made by the original holders to secure the listing, and who, on non-payment of the loans, were compelled to buy in the bonds held as security, were not, on the ground of fraud, entitled to priority over the original holders in the application of the pro-

road. Could there be any higher sanction than this? We think not. It would be an almost barbarous rule that would forbid a transaction of this character, and one that would at least hazard the undoing of all common transactions of mankind. Even in the cases where the equitable principle in question is given its widest scope, the general rule is that the contract may be avoided at the election of the stockholders, or *cestui que trust*, upon the terms of restoring what the trustee or agent has parted with in the transaction. The principle underlying this doctrine is forcibly stated by FINCH, J., in Duncomb *v.* N. Y., H. & N. R. R. Co., 84 N. Y. 190, where it is said: 'Nor is it at all questioned that in such cases the right of the beneficiaries, or those claiming through them to avoidance, does not depend upon the question whether the trustee in fact has acted fraudulently or in good faith and honestly, but is founded upon the known weakness of human nature, and the peril of permitting any sort of collision between the personal interests of the individual and his duties as trustee in his fiduciary character. Davoue *v.* Fanning, 2 Johns. Ch. 260. But the rule was adopted to secure justice, not to work injustice; to prevent a wrong, not to substitute one wrong for another, and hence have arisen limitations upon its operation calculated to guard it against evil results as inequitable as those it was designed to prevent. Thus, the beneficiary may avoid the act of the trustee, but cannot do so without restoring what it has received. York Co. *v.* Mackenzie, 8 B. Par. Cas. 42. To cling to the fruits of the trustee's dealing while seeking to avoid his act; to take the benefit of his loan and yet avoid and reverse its security, would be grossly inequitable and unjust. It would turn a rule, designed as a protection, into a weapon of offence and injustice.'"

ceeds of the foreclosure to the satisfaction of the bonds.[1] The United States Supreme Court has applied the doctrine that where negotiable paper has been put in circulation, and there is no infirmity or defense between the antecedent parties thereto, a purchaser of such securities is entitled to recover thereon as against the maker the whole amount, irrespective of what he may have paid therefor, in a case involving the following statement of facts: A railroad company contracted with a construction company to build and complete its railroad on a line designated on a map of the same, and to furnish and equip it, agreeing to pay for the same in stock and mortgage bonds to be issued from time to time as sections should be completed. A mortgage was made of the road and property then existing and afterwards to be acquired. The construction company began work and completed a small section, for which it received the stipulated pay in stock and bonds. It parted with the latter for a good consideration, and they eventually came by purchase into the possession of the bondholder, the trustees of whose estate brought the suit for the purpose of enforcing the mortgage lien. No further section was completed, but work was done at various points on the line, and the construction company acquired for the railroad company rights of way through nearly or quite the entire route. Subsequently another railroad company acquired these properties through the construction company, and completed the road. The court held that the bondholder, whose bonds were involved in the suit, being a *bona fide* holder of the bonds secured by the first mortgage, had through the mortgage a prior lien on the whole line for the full amount of the face of his bonds, which was not affected by the fact that the new company acquired its rights and property, not directly from the first company, but through intervening conveyances.[2] The railroad company here, in accordance

[1] Coe *v.* East & West R. Co. of Ala., (1892) 52 Fed. Rep. 531; Grant *v.* East & West R. Co. of Ala., (1892) 52 Fed. Rep. 531.

[2] Wade *v.* Chicago, Springfield & St. Louis R. R. Co., (1893) 149 U. S. 327; s. c., 13 Sup. Ct. Rep. 892. Mr. Justice JACKSON, for the court, said: "The bonds were valid securities in the hands of the trustee for the protection of Wade as accommodation indorser for Wing or the construction company, by whom they were pledged, and the pledgee or purchaser thereunder succeeded to the rights of the pledgor, and upon no principle could such purchaser, as against the maker, be restricted to what he might pay for the bonds. Negotiable securities once put in circulation for value may be transferred for less than their face, but the maker and those claiming under

with resolutions of the stockholders authorizing the issuance of consolidated first mortgage bonds, all the stockholders assenting, in order to extend and improve the road, to take up and retire the first mortgage bonds and debenture bonds, and to cancel the first and debenture mortgages, issued to the holders of the latter consolidated first mortgage bonds, and took up at an agreed rate the debenture bonds purchased by those holders, and stock issued to them and to the iron company, and the first mortgage bonds and stock issued to the construction company, and subsequently sold to those holders by the construction company to enable it to complete the road. It was held in the action to foreclose the consolidated first mortgage, that subsequent purchasers from those holders of bonds of some of these consolidated first mortgage bonds were chargeable with notice of the prior bonds and mortgages, and of the terms on which the consolidated bonds were issued, and that, the railroad company acquiescing in the transaction, and no intention to defraud subsequent creditors being shown, these subsequent purchasers of the bonds could not impeach the prior indebtedness on which the bonds were issued, in order to invalidate the balance of the consolidated bonds held by the original parties.[1]

him cannot limit the right of a subsequent holder to a recovery of what he may have paid therefor. In the case of Cromwell *v.* County of Sac, 96 U. S. 51, 60, in which it was held that the holder of such negotiable securities, regularly issued, is not limited to the amount which he may have paid therefor, it is said by the court, speaking by Mr. Justice FIELD: 'We are of opinion that a purchaser of a negotiable security before maturity, in cases where he is not personally chargeable with fraud, is entitled to recover its full amount against its maker, though he may have paid less than its par value, whatever may have been its original infirmity. We are aware of numerous decisions in conflict with this view of the law, but we think the sounder rule, and one in consonance with the common understanding and usage of commerce, is that the purchaser, at whatever price, takes the benefit of the entire obligation of the maker. Public securities, and those of private corporations, are constantly fluctuating in price in the market, one day being above par and the next below it, and often passing within short periods from one-half of their nominal to their full value. Indeed, all sales of such securities are made with reference to prices current in the market, and not with reference to their par value. It would introduce, therefore, inconceivable confusion if *bona fide* purchasers in the market were restricted in their claims upon such securities to the sums they had paid for them.'"

[1] Coe *v.* East & West R. Co. of Ala., (1892) 52 Fed. Rep. 531. It was said by the court: "The holders of the first consolidated bonds are charged with notice of the prior bonds and

A railroad corporation will not be allowed to show that restrictions imposed by its charter on its power to issue bonds were violated as against a *bona fide* holder of bonds issued by it, as such corporations, in general, have power to issue bonds.[1] The fact that bonds of a corporation which were legally pledged by authority of the directors for the purpose of carrying on construction work were, on foreclosure of the pledge, sold for a small amount, has been held not to affect the purchaser's title, no fraud being shown.[2] The remedies provided in a railroad mortgage given simultaneously with the issuing of the bonds for the better securing of which it is executed, will not affect the right of the bondholder to sue upon his bond at law, unless the provisions of the mortgage exclude this right of the bondholder in express terms or by necessary implication.[3] That it may be provided in a mortgage securing the bonds of a corporation that upon default in the interest the principal sum may be declared due, will not entitle the bondholder to sue upon his bond for the principal as due in case of default in interest. Such provisions have been held to apply only to the right to foreclose the mortgage.[4] It has

mortgages, and of the terms upon which their own bonds were issued. Caylus *v.* Railroad Co., 10 Hun, 295; Bronson *v.* Railroad Co., 2 Wall. 287, 311. This being the case, it is very doubtful whether complainants can impeach the indebtedness which existed prior to the issuance of their bonds, and upon which their bonds are based. At the time the first consolidated bonds were authorized and issued every interest consented, every bondholder, every stockholder, and the board of directors, and, so far as the record shows, every creditor; and the transaction was the consolidation of two series of bonds secured by mortgages of different dates into an equal number of bonds running a longer time, and bearing the same rate of interest, secured by one mortgage on practically the same property. Any and all the defects of construction, and all equities existing to the prejudice of the prior bonds, were waived and extinguished, and it was competent for the railroad company to make such waiver. See Bronson *v.* Railroad Co., *supra.* Even if the railroad company had been wronged or cheated, it would seem that subsequent creditors and subsequent purchasers have no right to question the transaction as long as the railroad company acquiesces, and no intention to defraud subsequent creditors is shown. See Graham *v.* Railroad Co., 102 U. S. 148. And the same case denies, in respect to such matters, that a corporation stands on any different footing from an individual debtor."

[1] Ellsworth *v.* St. Louis, Alton, etc., R. R. Co., 98 N. Y. 553; s. c., 33 Hun, 7.

[2] Wheelwright *v.* St. Louis, N. O. & O. Transportation Co., (1893) 56 Fed. Rep. 164.

[3] Manning *v.* Norfolk Southern R. Co., 29 Fed. Rep. 838.

[4] Mallory *v.* West Shore Hudson River R. R. Co., 3 Jones & S. 174; American Nat. Bank *v.* American Wood

been held in the United States Circuit Court for the southern district of Illinois that where overdue railroad mortgage bonds which belonged to the railroad company, were bought at forty cents on the dollar from the vice-president of the company after suit to foreclose the mortgage had been begun and a receiver had taken possession of the mortgaged property, the purchasers of such bonds were not *bona fide* holders, where inquiry on their part would have shown that the vice-president had no authority to sell the bonds.[1] It appearing in a suit to enforce the collection of railroad bonds which had been declared fraudulent that the bonds were given to a firm of which plaintiff was a member, in payment for work alleged to have been done for the railroad company, and that another member of the firm was an active participant in the fraud which rendered the bonds invalid, it was held that plaintiff was not an innocent holder.[2] In this suit to enforce the mortgage given by the corporation defendant there was an intervention by one who petitioned as the holder of certain bonds of the corporation for a recovery and a participation

Paper Co., (R. I.) 32 Atl. Rep. 305. As to the right to recover on bonds issued, secured by a mortgage, though the corporation had no power to execute the mortgage, see Philadelphia & Sunbury R. R. Co. *v.* Lewis, 33 Pa. St. 33. That it may be proven by extrinsic evidence that certain bonds were the ones secured by a mortgage, see Butler *v.* Rahm, 46 Md. 541. As to bonds payable to a payee named "or assigns," see Bunting *v.* Camden & Atlantic R. R. Co., 81 Pa. St. 254. As to the right of a holder to fill in his name in a bond issued and delivered in blank as to the payee, and bring suit in his own name, see White *v.* Vermont & Massachusetts R. R. Co., 21 How. 575; Chapin *v.* Vermont & Massachusetts R. R. Co., 8 Gray, 575. As to the rights of a purchaser of bonds which may have been pledged for a loan by the corporation, see Grand Rapids & Indiana R. R. Co. *v.* Sanders, 54 How. Pr. 214. Of one who may have purchased stolen bonds, see Maas *v.* Missouri, Kansas & Texas Ry. Co., 11 Hun, 8. As to the effect upon a purchaser of bonds being overdue when he purchases them, see Vermilye *v.* Adams Express Co., 21 Wall. 138. As to the purchaser of bonds referring to the mortgage securing being bound by the statements contained in the mortgage, see Caylus *v.* New York, K. & S. R. R. Co., 10 Hun, 295. As to the rights of holders of bonds by their terms convertible into stock of the corporation issuing them, see Denney *v* Cleveland & Pittsburg R. R. Co., 28 Ohio St. 108; Sutliff *v.* Cleveland & Mahoning R. R. Co., 24 Ohio St. 147. When the issuing of such bonds will be enjoined, see Belmont *v.* Erie Ry. Co., 52 Barb. 637; Ramsey *v.* Erie Ry. Co., 38 How. Pr. 193.

[1] American Loan & Trust Co. *v.* St. Louis & Chicago Ry. Co., (1890) 42 Fed. Rep. 819.

[2] Smith *v.* Florida Central & Western R. R. Co., (1890) 43 Fed. Rep. 731.

in the security. It appeared that one acting as the agent of the intervener in loaning her money had fraudulently procured the making of a note by an irresponsible party payable to himself "as trustee," and, having connection with the corporation defendant, had fraudulently put in circulation these particular bonds, which he forwarded to her as collateral security for the payment of the note with the note not indorsed, she merely obtaining by the transfer an equitable title to the note. This note the federal court held was subject to equitable defenses in the hands of the petitioner, and that the fact that the note was held subject to equitable defenses rendered the bonds payable to bearer subject also to such defenses while in her hands as the note holder as collateral security for the note.[1] The United States Circuit Court for the district of Washington has sustained its jurisdiction to entertain the bill of a bondholder secured by the mortgage of a street railroad company's property to enjoin the construction of a sewer by the city which had granted the franchise to use its streets to the railroad company, holding that a mortgage upon a street railroad was as much entitled to protection from unlawful injury by such action on the part of a city as any other kind of property.[2]

§ 501. Holders of income bonds — rules as to an accounting with them.— Where mortgage bondholders seek an accounting by a railway company, the bonds of which they hold, the company will not be allowed to charge against income any payment or loss arising out of an antecedent debt; and the holder of

[1] Thomson-Houston Electric Co. *v.* Capitol Electric Co. (Read, Intervener), (1893) 56 Fed. Rep. 849, dismissing the intervener's petition. See Farmers' Loan & Trust Co. *v.* Oregon & W. T. R. Co. (Congdon, Intervener), (1893) 58 Fed. Rep. 639, where a contract for the sale of railroad bonds was held to include overdue coupons, it appearing that the contract contemplated a purchase of the railroad free from all indebtedness, and that the purchase of the bonds was merely a means to that end. It was also held that the intervener, who took an assignment of these overdue coupons with knowledge of the contract above referred to, was not a *bona fide* purchaser.

[2] Clapp *v.* City of Spokane, (1892) 53 Fed. Rep. 515; citing Morgan *v.* Gilbert, 2 Fed. Rep. 835–838. When the rights of bondholders are not affected by a subsequent fraudulent issue, see Union Trust Co. of New York *v.* Nevada & O. R. R. Co., 20 Fed. Rep. 80. As to the right of the holder of a bond guaranteed by another corporation to recover upon default in payment by the one issuing the bond of the guarantor, see Harrison *v.* Union Pac. Ry. Co., 13 Fed. Rep. 522. When bondholders are entitled to money

coupons upon such bonds will be entitled to have the interest earned during each interest period applied upon the coupons representing that period.[1] Where a corporation has paid a higher rate of interest than needful on incumbrances prior to an income mortgage in an accounting in favor of the income bondholders, the corporation cannot charge the difference in interest against the income to the injury of the bondholders, in direct contravention of the provisions of the mortgage securing their bonds.[2] In an accounting between a railway corporation and the holders of its income bonds, where there was a provision made on the part of the corporation for retiring a series of secured income bonds and issuing new bonds in exchange, the bonds surrendered to be held by a trust company uncanceled until all were retired, a bondholder, who has not consented to surrender his bonds, would not be entitled in the accounting under the mortgage, to claim for interest due him more of the income than his share would have been had no bonds been surrendered.[3] The income mortgage bonds of a railway corporation in a New York case, issued after first consolidated mortgage bonds, were secured only so far as the principal of them was concerned, by the mortgage, the interest on them being payable out of net earnings as determined by the directors of the corporation. The Court of Appeals held that the directors of the corporation had the right, as against these income bondholders, to pay the bonds of a road leased by it, and the income bondholders had no lien on the road for the payment of their interest, and were bound by the decision of the directors as to net earnings.[4] Where an income mortgage to secure the payment of interest on income bonds was executed to cover the income of several roads constituting a system, and the company afterwards acquired additional roads, in a bill for accounting, it was held that the income fund referred to in this mortgage was confined to that of the roads specifically mentioned in the mortgage and not to that from the additional roads secured after its execution; that this was the income fund to which these bondholders were

coming into the hands of their trustees for their bonds, see Dwight *v.* Smith, 13 Fed. Rep. 50.

[1] Barry *v.* Missouri, Kansas, etc., Ry. Co., 27 Fed. Rep. 1.

[2] Barry *v.* Missouri, Kans. & Tex. Ry. Co., 34 Fed. Rep. 829.

[3] Barry *v.* Missouri, Kans. & Tex. Ry. Co., 34 Fed. Rep. 829.

[4] Day *v.* Ogdensburg & Lake Champlain R. R. Co., 107 N. Y. 129; 13 N. E. Rep. 765.

to look for the payment of their interest; that it was the duty of the company to keep separate accounts of the income and expenses of the different lines, and that it could not charge to the earnings of these specified lines of road the expenses or losses incurred in operating the additional lines of road acquired after the mortgage was given.[1]

§ 502. **Detached, uncanceled coupons — rules governing.** — When a third party with his own money takes up maturing coupons on bonds of a corporation, without knowledge of the holders, it is a question of fact, to be determined by the proof, whether it is intended to be a payment or a purchase which leaves the coupons outstanding. The coupons in this case having been dishonored before they came into the hands of the appellants, were subject in their hands to all defenses which existed against their assignor; and, it being evident that, without the knowledge of the holders of the bonds of this water works company, to which these coupons were attached, he used his money to pay the coupons on bonds which had been sold solely in order to enable him to float the rest of the issue, the Supreme Court of the United States held that it would be inequitable to allow him either a preference over those to whom he had sold the bonds or co-equal rights with them.[2] In a case before the Supreme Court of Michigan it appeared that the wife of a former promoter and president of a railroad company was bringing a suit against this company upon certain coupons which were past due and detached from bonds formerly issued by this company. The husband,

[1] Spies *v.* Chicago & Eastern Iowa Ry. Co., 40 Fed. Rep. 34.

[2] Wood *v.* Guarantee Trust & Safe Deposit Co., (1888) 128 U. S. 416; s. c., 9 Sup. Ct. Rep. 131. The court distinguished Ketchum *v.* Duncan, 96 U. S. 659, relied upon to support the denial that these coupons had been in fact paid. They said: "In Ketchum *v.* Duncan stress was laid on these circumstances, viz., that the persons alleged to have paid the coupons had no connection with the company issuing the coupons, or interest in it; that they had repeatedly and publicly notified the holders of the bonds and coupons that the coupons were to be purchased and not paid, and that the coupons were carefully received and preserved uncanceled." In Fidelity, etc., Company *v.* West Penn., etc., R. Co., (1891) 138 Pa. St. 494; s. c., 21 Atl. Rep. 21; 27 W. N. C. 267, the Supreme Court of Pennsylvania held that when interest coupons of mortgage bonds have been presented and paid at the place of payment, with money furnished by a third party, a private arrangement between such third party and the mortgagor that the transaction should be treated as purchase of the coupons by the former was not enforceable against the bondholders.

upon the idea that the bonds would sell better if they showed no unpaid past due coupons, had his wife clip them, and passed them to her without any consideration. He then sold those bonds with stock, he being the majority holder of the bonds and stock of the company, to a capitalist in New York that the latter might have control of the property. This capitalist afterwards sold the bonds and stock to one who was acting for the railroad company, complainant in the bill to enjoin the action upon these detached coupons. The parties in these various negotiations supposed that the sale of the bonds covered all the coupons attached and detached and not paid and canceled. Upon a review of the testimony in the case the Supreme Court held that such intention must prevail against the wife of the former president of the company, who was not an innocent purchaser for value, and that the coupons delivered to her must be considered as paid when cut from the bonds and so delivered.[1]

§ 503. **Actions on coupons — rules governing.** — A suit may be brought by the holder of overdue coupons and interest warrants, whether attached to or detached from corporation mortgage bonds, payable to bearer, and he may recover interest from the time they become payable.[2] An action in *assumpsit* may be brought by dissenting bondholders for the amount of unpaid

[1] Chicago & Grand Trunk Railway Co. *v.* Turner, (1889) 79 Mich. 133. For rules as to whether coupons detached from bonds and taken up are to be considered as paid or transferred, see Ketchum *v.* Duncan, 96 U. S. 659; Duncan *v.* Mobile & Ohio R. R. Co., 3 Woods, 567; Hand *v.* Savannah & Charleston R. R. Co., 17 S. C. 219; Miller *v.* Rutland & Wash. R. R. Co., 40 Vt. 399.

[2] Phil. & Read. R. R. Co. *v.* Smith, 105 Pa. St. 195; Phil. & Read. R. R. Co. *v.* Fidelity Ins. Trust, etc., Co., 105 Pa. St. 216. As to interest being recoverable on coupons overdue, see Ashuelot R. R. Co. *v.* Elliot, 57 N. H. 397; Langston *v.* South Carolina R. R. Co., 2 S. C. 248; Welsh *v.* St. Paul & P. R. R. Co., 25 Minn. 314; Gibert *v.* Wash. City, Va. Midland & Great So. R. R. Co., 33 Gratt. 586; Virginia *v.* Chesapeake & Ohio Canal Co., 32 Md. 501; North Pennsylvania R. R. Co. *v.* Adams, 54 Pa. St. 94. As to the negotiability of coupons, see Chesapeake & Ohio Canal Co. *v.* Blair, 45 Md. 102; Gilbough *v.* Norfolk & P. R. R. Co., 1 Hughes. 410; Haven *v.* Grand Junction R. R. & Depot Co., 109 Mass. 88; Hinckley *v.* Union Pac. R. R. Co., 129 Mass. 52; Evertson *v.* National Bank of New York, 66 N. Y. 14. As to actions on coupons, see Clark *v.* City of Janesville, 1 Biss. 98; Stevens *v.* N. Y. & Oswego Mid. R. R. Co., 13 Blatchf. 412; Burroughs & Springs *v.* Comrs., etc., 65 N. C. 234; City *v.* Lamson, 9 Wall. 477; County of Beaver *v.* Armstrong, 44 Pa. St. 63; Crosby *v.* New London, etc., R. R. Co., 26 Conn. 121; Clark *v.* Iowa City, 20 Wall. 583; Fitchett *v.* No. Pa. R. R. Co., 5 Phil. 132; Gelpcke *v.* City of

and overdue coupons upon their bonds notwithstanding the fact that a majority in interest of the bondholders secured by a mortgage may have consented to waive the rights secured by the mortgage.[1] The right of a bondholder to bring an action at law to recover on overdue interest coupons will not be affected by a provision in the mortgage executed by the corporation securing the bonds forbidding the holders of the bonds from proceeding at law or in equity to foreclose it, or procure a sale of the property independently of the trustee, although the mortgage provide for its foreclosure on default in the payment of the coupons.[2] Neither will the rights of the bondholder to such action at law upon his overdue interest coupons be affected by a waiver of the right to foreclose the mortgage on default in the payment of the interest coupons attached to the mortgage secured by it.[3] The Pennsylvania Supreme Court has declared these rules in actions upon coupons detached from bonds of a corporation secured by mortgage: Where an action is brought upon coupons it is not necessary to prove the execution of the mortgage securing the bonds to which the coupons were attached, particularly where a rule of court providing for an affidavit denying the execution of a writing sued upon has not been complied with. Recovery may be had upon coupons signed by the vice-president of the company, although the mortgage accompanying the bond provided that the bond should be signed by the president.[4] Where no affidavit has been filed denying proper execution, as provided by rule of court, evidence that the coupons were not properly executed will be excluded at the trial. And evidence that plaintiff entered into a written agreement with other creditors that they would take stock in the corporation for the principal of their debts is inadmissible.[5] The Statute of Limitations cannot be set up to prevent a recovery upon coupons which have not been detached from bonds; nothing can avail to defeat a recovery

Dubuque, 1 Wall. 175; Grand Rapids & Ind. R. R. Co. *v.* Sanders, 54 How. Pr. 214; Kennard *v.* Cass County, 3 Dill. 147; McCoy *v.* Washington County, 3 Wall. Jr. 381; McLendon *v.* Comrs., 71 N. C. 38; Nat. Exchange Bank *v.* Hart., Prov. & F. R. R. Co., 8 R. I. 375; Whitaker *v.* Hart., Prov. & F. R. R. Co., 8 R. I. 47; Welsh *v.* St. Paul & Pac. R. R. Co., 25 Minn. 314.

[1] Manning *v.* Norfolk Southern R. Co., 29 Fed. Rep. 838.

[2] Lyon *v.* New York, S. & W. R. Co., 14 Daly, 489.

[3] Ibid.

[4] Conshohocken Tube Co. *v.* Iron Car Equipment Company, (1894) 161 Pa. St. 391.

[5] Roberts & Co. *v.* Iron Car Equipment Co., (1894) 161 Pa. St. 348.

upon them but the presumption of payment which the law allows at the end of twenty years; and such presumption may be rebutted by evidence of non-payment.[1] In a case where bonds were issued by a railroad company, with interest payable annually, July first, with a provision that in case the net earnings of a portion of its road were not sufficient to pay the interest, scrip might, at the option of the company, be issued for it. In the absence of an exercise of the option by the company to issue the scrip for interest, as provided for, a federal court held that the holder of the bonds had an immediate right of action for his interest; it was also held that the acceptance of scrip for interest during some of the years by the bondholders did not amount to a waiver so as to prejudice this bondholder's rights in an action for interest on his bonds for subsequent years; further, that where the treasurer of the railroad company, shortly after the interest was due in these subsequent years, had notified the bondholders that the company could not pay the interest, but no action was taken as to the scrip, no demand on the part of this bondholder for the payment of his interest was necessary before action to entitle him to a recovery.[2]

§ 504. Guaranty of bonds of one corporation by another — rules.—A railroad corporation, vested with power by its charter to issue its own bonds, may guarantee the bonds of another railroad corporation received by it in payment of a debt, and sold for value or transferred in payment of its own debts, such guaranty being given to improve the credit of the bonds or to obtain an adequate price for them.[3] In this foreclosure suit there was presented to the United States Circuit Court of Appeals the question whether a land company, a corporation which guaranteed the mortgage bonds of the railroad company, defendant in the suit, and afterwards joined the railroad company in borrowing money with which to pay the interest coupons upon these bonds, should not have been a party to this suit. The appellate court held that by this original guaranty and borrowing in connection with the railroad company the money to pay the interest coupons

[1] Phila. Trust Co. *v.* Phila. & Erie R. R., (1894) 160 Pa. St. 590.

[2] Texas & Pac. Ry. Co. *v.* Marlor, 8 Sup. Ct. Rep. 311.

[3] Rogers Locomotive & Machine Works *v.* Southern Railroad Association, 34 Fed. Rep. 278.

the land company did not become subrogated *pro tanto* to the rights of the mortgagee, so as to become an indispensable or even a proper party to the subsequent foreclosure suit, as subrogation does not take place until the payment of the whole debt for which the surety is liable. The contention of the appellant, it was argued, rested upon a provision in the charter of the railway company to this effect: "And in order to enable said company [the land company] to guarantee the punctual payment of the interest and principal of such bonds, it is hereby expressly declared that the guarantors of such bonds shall be entitled to all the benefits of such mortgage or deed of trust made to secure such bonds to the same beneficial extent that the holders of said bonds may be entitled." The appellate court held that this provision in the charter of the railway company was a mere declaration of the principles of subrogation, and could not be construed as placing the guarantors, who had made only a partial payment, upon an equal footing with the mortgage creditors.[1] The jurisdiction of a court of equity of a bill brought by a railroad corporation to cancel its guaranty upon the bonds of another corporation, on the ground of illegality and fraud, has been sustained by the United States Circuit Court for the district of Kentucky. The court held, in the first place, that the bill was not demurrable because it failed to show that the defendants were not *bona fide* holders for value, as when fraud or illegality on the inception of negotiable instruments is shown it devolves upon the indorsee to show that he is a *bona fide* holder. The main point on which the jurisdiction of the court was placed was that such a bill against the holders of the bonds to cancel the guaranty was maintainable in equity on the ground of preventing a multiplicity of suits, although it might have a good defense at law to each of the bonds.[2]

[1] Columbia Finance & Trust Co. *v.* Kentucky Union Ry. Co., (1894) 60 Fed. Rep. 794. The court distinguished Railroad Co. *v.* Schutte, 103 U. S. 141.

[2] Louisville, N. A. & C. Ry. Co. *v.* Ohio Valley Improvement & Contract Co., (1893) 57 Fed. Rep. 42. The guaranty of the railroad company was alleged to have been indorsed upon the bonds of the improvement company illegally and fraudulently. LURTON Circuit Judge, reviewed cases involving the principles as follows: "The case of Railway Co. *v.* Schuyler, 17 N. Y. 592, is an interesting and instructive case. In that case it appeared that spurious certificates of stock in a railroad corporation had been issued by an officer having apparent authority to

§ 505. **Lease of a bonded railroad — when lessee is not bound on the bonds.**— An Iowa railroad company, by action of its directors, made a lease of its road to a second Iowa company for forty years. This latter company afterwards entered into a contract of its road and the leased road to an Illinois corporation, a railway company, for twenty years. The first-mentioned lessor company had, previously to the lease of its road, issued bonds which were sold and the proceeds used in the construction of its road, and executed a mortgage to certain trustees to secure these bonds. The mortgage covered the company's road, and the net earnings thereof, its franchises, privileges, right of way, depot grounds, and all material designed to be used in construction; also, "the rents and moneys payable by any person or company" to that corporation "for the use of said road and its appurtenances." By its contract with the lessee company the Illinois company assumed the lease made by this lessee with the lessor company. When the bonds were sold upon the market there was indorsed

do so, and undistinguishable on their face from certificates of genuine stock, and were outstanding in the hands of numerous holders. The holders of such spurious certificates were made parties defendant to the bill filed by the railroad company. After an elaborate consideration of the question, as to whether or not the bill would lie, that court maintained its jurisdiction and held that the false certificates, having a common origin and common ground of invalidity, though the holders became such under different circumstances and conveyances, and claimed different rights, yet they were all properly joined as defendants and the bill maintained as a bill to prevent a multiplicity of suits. In Supervisors *v.* Deyoe, 77 N. Y. 219, we find a similar case. The treasurer of Saratoga county, under an authority to issue notes for money advanced to the county to the amount of some $20,000, issued seventy-three notes to the amount of one hundred and thirty-eight thousand dollars. These notes were held by fifty-three persons, many of whom had brought separate suits upon their notes. The supervisors filed a bill in equity against all the holders of said notes, including those who had brought suits at law. Upon demurrer to the bill it was held that upon the facts a case was made entitling the plaintiff, upon equitable principles, to implead the holders of the notes for the purpose of having their respective rights and the liability of the [county?] determined in one action; that the claims were of the same general character, and that the action was maintainable for the purpose of preventing a multiplicity of suits and to protect plaintiff against the hazard of a double recovery. The case of Waterworks *v.* Yeomans, L. R., 2 Ch. App. 11, was this: A very large number of persons held separate claims against the waterworks company. The claims were for damages originating in an inundation resulting from the breaking of a reservoir. Under a special act commissioners were appointed to inquire into and assess these damages and issue certificates

upon them and signed by the president of the lessor company this statement: "The lease of the [lessor company's road] to the [first-named lessee], referred to in the within bond, has this day been assumed by the [Illinois railroad company], and the minimum rent which that company has thereby obligated to pay in monthly installments is more than sufficient to meet the entire amount of interest on this issue of bonds." The road of the mortgagee company went into the control of the Illinois company, which paid the fixed rental, but, having obtained control of the company during the term of lease from which it had leased the mortgaged road, at the end of the twenty years of its lease, returned the road to the second company. The surviving trustee of the mortgage of the lessor company brought a bill in equity, charging that the course of the Illinois company in neglecting to perform the covenants of its lease, and to account for the earnings and income of the mortgaged railroad, had caused the mortgagee to default in the payment of the bonds and coupons, and the mortgagee being insolvent and without resources, other than its leased property, had failed to collect and properly apply the income, rents and profits of the mortgaged property, and had misapplied some portions of them; and that a foreclosure and sale of the mortgaged property, before the obligation which the Illinois company had assumed, should be enforced, would be injurious to the mortgagee company and its stockholders, as well as the bondholders. The trustee sought to obtain, by a decree of the court, the control of the rents and income under the contract of lease. As to the Illinois company, the United States Circuit

upon the several claims. The waterworks claimed that the power of the commissioners had expired, and that a large number of these certificates were in consequence invalid. A bill by the company against a few as representing the whole number was filed and a demurrer sustained. The Court [of Appeals] held that as the rights of all depended upon the same question, and that, although the defense could be made at law, it was 'a very fit case, by analogy at least, to a bill of peace, for a court of equity to interpose and prevent the unnecessary expense and litigation which would be thus occasioned, and to decide once for all the validity or invalidity of the certificates upon which the claims of all persons depend.'" See, also, Black *v.* Shreeve, 7 N. J. Eq. 440. As to guaranty of bonds, see Low *v.* California Pac. R. R. Co., 52 Cal. 53; New Haven, M. & W. R. R. Co. *v.* Town of Chatham, 42 Conn. 465; Arnot *v.* Erie Ry. Co., 67 N. Y. 315; Toppan *v.* Cleveland, Col. & Cin. R. R. Co., 1 Flip. 74; Opdyke *v.* Pacific R. R. Co., 3 Dill. 55; Codman *v.* Vermont & Canada R. R. Co., 16 Blatchf. 165.

Court held that as the rentals for this road had been fully paid by that company to the mortgagee company to the date on which its road was surrendered to the original lessee before the commencement of the suit, there was no ground whatever for a decree against that corporation, and as to that company the original suit was ordered dismissed.[1]

[1] Jesup *v.* Illinois Central R. R. Co., (1890) 43 Fed. Rep. 483. It was further held that there was nothing in the indorsement made upon the bonds as to the assumption of the contract of lease by this company to estop it from denying its liability in this action.

CHAPTER XXVI.

MORTGAGES AND TRUST DEEDS — PRIVATE CORPORATIONS.

§ 506. Power of corporations to execute mortgages and trust deeds upon their property.

507. Statutes requiring assent of stockholders to mortgages construed.

508. Mortgages and trust deeds — rules to as place of execution, authorization — mode of execution, to whom executed, record, etc.

509. Estoppel of corporation to deny authority of officers to mortgage.

510. Effect of laches of corporation in repudiating a mortgage.

511. What are reasonable provisions in a mortgage.

512. Chattel mortgages of corporations.

513. Deeds of trust and mortgages securing directors — when properly given.

§ 514. The validity of mortgages as affected by restrictions, constitutional, statutory, or in charter upon indebtedness to be incurred.

515. A mortgage of corporation property to pay purchase-money debts.

516. Illustration of an equitable mortgage.

517. Mortgage of a consolidated railroad company — estoppel to claim its invalidity on the ground that the consolidation was not legally perfected.

518. Illustration of a fraudulent mortgage.

519. What corporation mortgages cover, and what they do not cover.

520. Trustees of such mortgages — their duty, rights and powers.

§ 506. Power of corporations to execute mortgages and trust deeds upon their property.— Corporations, it is well settled, have the power to sell their property, real and personal, and to mortgage it for the security of their debts, as an incident to the power of acquiring and holding such property. This right exists by common law, but may be limited by statute, or by the laws or charters under which such corporations are organized.[1]

[1] Fitch *v.* Lewiston Steam Mill Co., (1888) 80 Me. 34; s. c., 12 Atl. Rep. 732. See Pierce *v.* Emery, 32 N. H. 503; Richards *v.* Merrimack & Connecticut River Railroad, 44 N. H. 135. As to power to mortgage, see Thomas *v.* Citizens' Horse Ry. Co., 104 Ill. 462; McAllister *v.* Plant, 54 Miss. 106; Pullan *v.* Cin. & Chicago Air Line R. R. Co., 4 Biss. 35; Campbell *v.* Texas & N. O. R. R. Co., 2 Woods, 263; Branch, Sons & Co. *v.* Atlantic & Gulf R. R. Co., 3 Woods, 481; Coe *v.* Col., Piqua & Indiana R. R. Co., 10 Ohio St. 372; Central Gold Mining Co. *v.* Platt, 3 Daly, 263; Willink *v.* Morris Canal & Bkg. Co., 4 N. J. Eq. 377; Allen *v.* Montgomery R. R. Co., 11 Ala. 437; Covey *v.* Pittsburg, Ft. Wayne & Chicago R. R. Co., 3 Phil. 173; Dunham *v.* Isett, 15 Iowa, 284; Bardstown & Louisville R. R. Co. *v.* Metcalfe, 4 Metc. (Ky.) 199; Hays *v.* Galion Gas Light & Coal Co.

The United States Circuit Court of Appeals has held that an Ohio railway corporation may mortgage after-acquired property, acquired either by itself or by any successor in title exercising the same franchises or similar franchises granted by the same sovereign power.[1] A Pennsylvania railroad company was empowered by its charter to "purchase, receive, have, hold, and enjoy, to them and to their successors and assigns, lands, tenements, hereditaments, goods, chattels, and all estate, real, personal, and mixed, of what kind or quality soever, and the same from time to time to sell, mortgage, grant, alien or dispose of," etc. In a case before the Supreme Court of that state, the question was raised as to the power of this company to execute a mortgage upon its property. Referring first to the provision of the charter quoted above, the court said: "The power to mortgage is given in the most explicit language, and embraces all the property which the company may acquire or hold 'real, personal, and mixed, of what kind or quality soever.' It is difficult to conceive how there could be a larger or more comprehensive description of the kind of property upon which the power to mortgage could be exercised than is contained in these words. They embrace every species of property known to the law; and the power itself is not subjected to any limitations, restrictions or

29 Ohio St. 330; Kennebec & Portland R. R. Co. *v.* Portland & Kennebec R. R. Co., 59 Me. 9; Loudenslager *v.* Benton, 4 Phil. 382; McCurdy's Appeal, 65 Pa. St. 290; Miller *v.* Rutland & Washington R. R. Co., 36 Vt. 452; Ludlow *v.* Hurd, 1 Disney, 552; Mobile & Cedar Point R. R. Co. *v.* Talman, 15 Ala. 572; Racine & Mississippi R. R. Co. *v.* Farmers' Loan & Trust Co., 49 Ill. 331; Richards *v.* Merrimack & Connecticut River R. R. Co., 44 N. H. 127; Coe *v.* New Jersey Midland Ry. Co., 31 N. J. Eq. 105; McLane *v.* Placerville & Sacramento Valley R. R. Co., 66 Cal. 606; Duncomb *v.* New York, H. & N. R. R. Co., 84 N. Y. 190; Gordon *v.* Preston, 1 Watts, 385; Burt *v.* Rattle, 31 Ohio St. 116; Jackson *v.* Brown, 5 Wend. 590; Reynolds *v.* Stark County, 5 Ohio, 205; State *v.* Rice, 65 Ala. 83; Pennock *v.* Coe, 23 How. 117; Shaw *v.* Bill, 95 U. S. 10; Howe *v.* Freeman, 14 Gray, 566; Ellis *v.* Boston, H. & E. Railroad, 107 Mass. 1; Da Ponte *v.* Northern Pac. R. R. Co., 21 Blatchf. 534; Mead *v.* New York, H. & N. R. R. Co., 45 Conn. 199; Bell *v.* Chicago, St. L. & N. O. R. R. Co., 34 La. Ann. 785; Scott *v.* Clinton & S. R. R. Co., 6 Biss. 529.

[1] Compton *v.* Jesup, 68 Fed. Rep. 263. As to the power of a gas company to mortgage its entire property to secure bonds and floating indebtedness, see Hunt *v.* Memphis Gas Light Co., (Tenn.) 31 S. W. Rep. 1006. As to the limitations on the power of a railroad corporation under the New Jersey statutes to mortgage its property, see Baker *v.* Guarantee Trust & Safe Deposit Co., (N. J. Eq.) 31 Atl. Rep. 174.

qualifications of any kind. No provision is made as to the manner in which the power should be exercised, and hence no particular formalities were required to be observed. An authentic act of execution by the proper officers of the company would seem, therefore, all that was necessary to a valid exercise of the power. We cannot assent to the contention that, in addition to the power to mortgage, there must also be expressed a specific authority to borrow money and issue bonds therefor. The manifest purpose of a mortgage is to secure loans of money, and the power to borrow money and to give the ordinary evidences of loans in the form of bonds, or other obligations to the same effect, is a necessary incident to the power to mortgage. But it is also the necessary incident to the right to build a railroad; and it is only essential to have the power to mortgage expressly granted, in order that it may be exercised for the purpose of securing indebtedness, whether arising from loans of money or upon other considerations. Nothing to the contrary of this was decided in the case of Pittsburgh R. Co. *v.* Allegheny County, 63 Pa. St. 126. Additional power to mortgage was granted to this company by [the following] section of [a subsequent act of the legislature], in these words: 'And the said railroad company are hereby authorized to mortgage or otherwise incumber their said road and any real and personal estate which may belong to it, for the purpose of carrying out the privileges granted by the act and the several supplements thereto incorporating the same.'" The court said: "It was contended for the appellants that this power was limited to the purpose of carrying out the privileges granted by the incorporating and supplementary acts, and that those privileges were exhausted when the road as then built was finished. By [another] section of the same act the company was authorized to extend their road to any point they may select in [certain named] counties, so as to form a connection with [a certain named railroad], or any other railroad that may be constructed. Other powers of extension were granted by previous and subsequent legislation. The power to mortgage clearly included the railroad and all other real and personal estate of the company, without reference to the time of its acquisition, so long as the purpose was observed of carrying out the privileges of the company granted by the original act of incorporation, or any supplements thereto. So long as the acts done or supposed to be done are within the legalized powers of the company, whether

before or subsequent to the passage of this act, the power to mortgage attaches. We cannot agree that it was restrained to the mere physical structure then completed. If a subsequent acquisition of rolling stock should become necessary, or the erection or lawful acquisition of branches, in addition to those already possessed, should take place, it cannot be doubted that the power to mortgage, conferred by this act would be applicable."[1] A railroad company of Tennessee, the charter of which empowered it to mortgage for the purpose of completing its road and equipping it with everything necessary to give it full operation, was held by the Supreme Court of that state not to be thereby authorized to execute bonds and mortgage for any other purpose than that of completing and equipping the original line of road authorized by the charter. They further held that a mortgage by this company, executed within twenty-five years after the completion and equipment of its road, and not purporting to have been executed for any such purpose, or to secure the renewal of bonds originally issued for those purposes, could not be presumed to have been executed for the purposes named in the charter.[2] The Supreme Court of the United States has held that a manufacturing corporation of New York, having authority to mortgage its property for the purpose of carrying on its business, is not prohibited by the laws of that state from executing such a mortgage to secure the payment of money to be thereafter advanced.[3]

[1] Gloninger *v.* Pittsburgh & Connellsville R. R. Co. 139 Pa. St. 13; s. c., 21 Atl. Rep. 211; 27 W. N. C. 497.

[2] Frazier *v.* East Tennessee, Va. & Ga. R. R. Co., 88 Tenn. 138; s. c., 12 S. W. Rep. 537. In Belden *v.* Burke, 72 Hun, 51; s. c., 25 N. Y. Supp. 601, it was held that no statute being contravened and the stockholders not resorting to any deception or fraud to attract investors to purchase the mortgage bonds, those who have acquired all the stock of a corporation had a legal right to cause the corporation to mortgage its property in an amount exceeding its value. See Brown *v.* Supply Co., 23 Or. 541; Nelson *v.* Hubbard, 96 Ala. 238; Adams Cotton Mills *v.* Dimmick, 96 Ala. 238; Grant *v.* Railroad Co., 13 U. S. App 1; s. c., 4 C. C. A. 511; Robinson *v.* Land Co., 2 Colo. App. 17.

[3] Jones *v.* Guaranty & Indemnity Co., (1879) 101 U. S. 622. Mr. Justice SWAYNE, speaking for the court, said, as to the power of corporations respecting the execution of mortgages: "At the common law every corporation had, as incident to its existence, the power to acquire, hold and convey real estate, except so far as it was restrained by its charter or by act of parliament. This comprehensive capacity included, also, personal effects of every kind. The *jus disponendi* was without limit or qualification. It extended to mortgages given to secure the payment of debts. 1 Kyd

The Court of Appeals of New York in a fully considered case has sustained the validity of a mortgage given by a manufacturing corporation covering all of its real and personal property. In this case RAPALLO, J., has thus stated the views of that court as to the construction of the statutes of that state of 1864 and 1871 on the subject and the powers conferred by them on the corpora-

Corp. 69, 76, 78, 108; Ang. & A. Corp. § 145; 2 Kent Com. 282; Reynolds *v.* Commissioners of Stark County, 5 Ohio, 204; White Water Valley Canal Co. *v* Vallette, 21 How. 414. A mortgage for future advances was recognized as valid by the common law. Gardner *v.* Graham, 7 Vin. Abr. 22, pl. 3. See, also, Brinkerhoff *v.* Marvin, 5 Johns. Ch. 320; Lawrence *v.* Tucker, 23 How. 14. It is believed they are held valid throughout the United States, except where forbidden by the local law. The statute under which the oil company [the mortgagor] came into existence made it 'capable in law of purchasing, holding and conveying any real and personal estate, whenever necessary to enable' it to carry on its business, but it was forbidden to 'mortgage the same or give any lien thereon.' This disability was removed by the later act of 1864, which expressly conferred the power before withheld. This change was remedial, and the clause which gave it is, therefore, to be construed liberally with reference to the ends in view. The learned counsel for the appellant insisted that a mortgage could be competently given by the oil company only to secure a debt incurred in its business and already subsisting. This, we think, is too narrow a construction of the language of the law. A thing may be within a statute but not within its letter, or within the letter and yet not within the statute. The intent of the lawmaker is the law. People *v.* Utica Insurance Co., 15 Johns. 357; United States *v.* Babbit, 1 Black, 55. The view of the court in Thompson *v.* New York & Harlem Railroad Co., 3 Sandf. Ch. 625, was sounder and better law. There the charter authorized the corporation to build a bridge. It found one already built that answered every purpose and bought it. The purchase was held to be *intra vires* and valid. Here the object of the authorization is to enable the company to procure the means to carry on its business. Why should it be required to go in debt, and then borrow, if it could, instead of borrowing in advance, and shaping its affairs accordingly? No sensible reason to the contrary can be given. If it may borrow and give a mortgage for a debt antecedently or contemporaneously created, why may it not thus provide for future advances as it may need them? This may be more economical and more beneficial than any other arrangement involving the security authorized to be given. In both these latter cases the ultimate result with respect to the security would be just the same as if the mortgage was given for a pre-existing debt in literal compliance with the statute. No one could be wronged or injured, while the corporation, whom it was the purpose of the law to aid, might be materially benefitted. Is not such a departure within the meaning, if not of the letter, of the statute? There would be no more danger of the abuse of the power conferred than if it were exercised in the manner insisted upon. The safeguard provided

tion in these words: "Where money is lent to an individual or to a corporation authorized to borrow money, and the borrower at the time of the loan delivers his bond and mortgage as security for the repayment of the money so loaned, it can hardly be questioned that the bond and mortgage are given to secure a debt contracted by the borrower. [These statutes] declare that where the requisite consent of stockholders is given, the mortgage shall

in the required assent of stockholders would apply with the same efficacy in all the cases. The object of the loan, the application of the money, and the restraints imposed by the charter in those particulars, would be the same whether the transaction took one form or the other. According to our construction the company could give no mortgage but one growing out of their business, and intended to aid them in carrying it on. In legal effect the difference between the two constructions is one merely of mode and manner, and not of substance. Such securities are not contrary to the law or public policy of the state [of New York]. Many cases are found in her reported adjudications where both judgments and mortgages for future advances have been sustained. Our view is not without support from the language of the statute, that 'every mortgage so made shall be as valid to all intents and purposes as if executed by an individual owning such real estate.' If this mortgage had been given by individuals, the question we are examining doubtless would not have been brought before us for consideration. * * * When a deed is fatally defective for the want of a sufficient consideration to support it, such a consideration subsequently arising may cure the defect and give the instrument validity. Sumner *v.* Hicks, 2 Black, 532. It is not necessary to go through the form of executing a second deed to take the place of the first one. This principle applies to the mortgage after all the advances had been made, conceding that it had before been invalid for the reason insisted upon. The statute of 1864 neither expressly forbids nor declares void mortgages for future advances. If the one here in question be *ultra vires*, no one can take advantage of the defect of power involved but the state. As to all other parties, it must be held valid, and may be enforced accordingly. Silver Lake Bank *v.* North, 4 Johns. Ch. 370; National Bank *v.* Matthews, 98 U. S. 621. In the latter case this subject was fully examined. A corporation can act only by its agents. If there were any such technical defect as is claimed touching the execution of this mortgage, it has been cured by acquiescence and ratification. No no else can raise the question. All other parties are concluded. Gordon *v.* Preston, 1 Watts (Pa.), 385. Where money had been obtained by a corporation upon its securities, which were irregular and *ultra vires*, but the money was applied for the benefit of the company, with the knowledge and acquiescence of the shareholders, the company and the shareholders were estopped from denying the liability of the company to repay it. And the same result follows where such securities are issued with the knowledge of the shareholders, so far as the money thus raised is applied for the benefit of the company. In re Cork & Youghal Railway Co., Law Rep., 4 Ch. 748. A court of equity abhors forfeitures and will not lend its aid to enforce them. Marshall *v.* Vicksburg, 15 Wall. 146. Nor will it give its aid in the assertion

be as valid to all intents and purposes as if executed by an individual. The only other restriction is that the debt secured by the mortgage must be one contracted in the business for which the corporation was incorporated. There is nothing in the statute which requires that it should have been contracted at any particular time. If it is contracted simultaneously with the giving of the security, and is a legitimate debt incurred in the business of the company, it comes within the letter of the authority conferred by the statute which covers 'any debt which may be contracted by it in the business for which it is incorporated.' As to a mortgage given to secure future advances, different questions might arise, but where a bond secured by mortgage is given to the lender for money advanced at the time, the borrower becomes immediately indebted, and it would seem to be immaterial whether the money is applied by the borrower to the payment of some antecedent debt or to other purposes for which he was legitimately entitled to borrow the money. The only conceivable intent which could be attributed to the legislature of requiring that the power of mortgaging should be confined to the securing of debts other than those created simultaneously with the giving of the security would be to put it beyond the power of the trustees or directors, even with the assent of the stockholders, to borrow money not needed for the payment of previously existing debts, and thus obtaining the control of funds which they might misapply. I fail to find any language in the act expressive of such intent. It likens the power given to these corporations to that of an individual to mortgage his own property, to secure any debt which he may contract, and there is no restriction upon this power except that the assent of stockholders must be obtained." [1]

of a mere legal right contrary to the clear equity and justice of the case. Lewis *v.* Lyons, 13 Ill. 117."

[1] Lord *v.* Yonkers Fuel Co., (1885) 99 N. Y. 547. Referring to leading cases, it was said: "In Greenpoint Sugar Co. *v.* Whitin, 69 N. Y. 328, it is said by CHURCH, Ch. J., at page 333, that the act of 1864 removed the restriction substantially imposed by the act of 1848, with a proviso requiring only that those interested, the stockholders, should consent, thus plainly evincing that the purpose and intent were to protect the stockholders from improvident or corrupt acts by the officers of the company; that there is nothing showing that the legislative policy regarded the mortgaging of corporate property improper *per se*, but the policy adopted indicates a fear of its improper exercise and an intention to guard against it. And again at page 334, that the act of mortgag-

§ 507. Statutes requiring assent of stockholders to mortgages construed.—The act of the state of New York of 1867, with reference to the execution of mortgages by manufacturing corporations, was succeeded by a further amendatory act of the statute of 1848, the act of 1872, whereby such corporations were authorized to purchase, hold and convey any real or personal estate necessary to enable them to carry on their cor-

ing is not deemed illegal, but the principal must assent in writing. In that case the mortgage was given to secure the purchase price of real estate conveyed to the company by the mortgagee on the same day the mortgage was executed, but which had been previously occupied by the company under a contract of purchase. In Rochester Savings Bank *v.* Averell, 96 N. Y. 467, the mortgage was given to secure $10,000 borrowed by the company from the bank at the time of the execution of the mortgage. The feature existed in that case that the money was borrowed to pay certain debts of the company and was so applied. The question did not arise in that case as to what the result would have been in the absence of that feature. Adopting the comparison suggested by the statute, with the act of an individual mortgaging his own property to secure the payment of his own debt, and supposing the case of a principal, having an agent authorized to borrow money to be used in the business of the principal, and that the principal should under that state of existing circumstances give a power of attorney to the agent empowering him to secure the payment of 'any debt theretofore contracted, or which might be contracted by him in the business' of the principal, by mortgage on his real estate, can it be doubted that a mortgage given by the agent to secure money borrowed by him in the business of his principal, simultaneously with the giving of the mortgage security, would be within the terms of the power? I can see no reason for applying a different rule of construction to an authority in the same words contained in a statute. But in the present case we are not under the necessity of deciding that question or determining what the result would have been if the bonds had been sold, or money raised thereon by the company for purposes other than the payment of existing debts. It appears from the findings, not only that the money paid to the company for the bonds was used in the payment of its debts, but that the money was so paid by the bondholders to the company only as its other existing debts became due. The bonds secured by the mortgage did not acquire vitality until they were issued to purchasers paying value therefor, and did not until then become liens upon the mortgaged property. Consequently, when the mortgage lien was created, it was, as to each bond issued, created for the purpose of paying debts then owing by the company and was so applied. There is nothing in the act which requires that in the case of a trust mortgage to secure negotiable bonds to be thereafter issued, the debts authorized to be secured should be in existence at the time the mortgage and bonds are prepared and executed. Every conceivable intent of the statute is effectuated, provided the bonds are negotiated only for the purpose of securing or paying debts contracted before the negotiation of the bonds. Where a

porate operations, and also to borrow such sums of money, not exceeding one-half of their capital, as might be necessary to carry on their business, and to issue and dispose of their bonds for any amount so borrowed and mortgage the corporate property and franchises of the company to secure the payment of any debt contracted by it for the purposes aforesaid. The Court of Appeals held that the obvious effect of the last act was to supersede the provisions of the law of 1867 requiring the assent of two-thirds of the stockholders of a corporation as a condition to the exercise of the right to mortgage and to enlarge the power of a corporation to mortgage, so as to include personal property and franchises as well as real estate, and to cover the payment of all debts contracted for the legitimate operations of the corporation. In this particular case a gas light company purchased the property described in the mortgage of the plaintiff, agreeing to pay therefor $50,000 in cash and $200,000 in the stock of the company, and he accepted the mortgage in lieu of the cash payment. The court held it was competent for him to do so without impairing the validity of the mortgage, and for the company to transfer the mortgage to him in lieu of the money which it was authorized to borrow for the purpose of making such payment. "The result," it was said, "accomplished by this transaction was the precise equivalent of a delivery to a creditor to secure a loan, and did not constitute a diversion of the mortgage from its intended object. The agreement of purchase created a debt, and the purpose of its creation being to enable the company to carry on its business operations, the transaction was brought within the terms of the statute authorizing such a corporation to mortgage its property." Again it is said: "The power to purchase property for the purposes of the corporation, and, if necessary, to contract

bond of this description, having no previous vitality, is delivered to a creditor of the company to pay or secure his debt, the delivery of the bond is the act by which his debt becomes secured. The security to the creditor then for the first time comes into being, and is as effectual as if the mortgage were executed at the same time with the delivery of the bonds. The effect is the same if the bond is sold to provide means to pay a debt existing at the time of the sale, and the proceeds are paid to the creditor. As held in the case of Carpenter *v.* Black Hawk Co., 65 N. Y. 43, the statute prescribes no form in which the mortgage shall be made. The mode in which the mortgage lien shall be created is left to the company. All that is required is that the lien should be given to secure a legitimate debt of the corporation, and any appropriate and convenient form for accomplishing that end may be adopted."

a debt therefor, is expressly given to the corporation, and authority to mortgage its property for the payment of such debt is clearly within the spirit as well as the letter of the statute."[1] Bills in equity were filed, one by a stockholder and others by unsecured simple contract creditors, in a court of Massachusetts to prevent the sale under power in a trust deed or mortgage of the property of a heating company, a corporation of that state, given to secure certain bonds which the heating company had issued and used in securing advances of money for carrying out its purposes. This brought in question the power of such a corporation in that state to make a mortgage such as it had executed in these cases. The Supreme Judicial Court held that the heating company was clothed with power under the laws of Massachusetts to execute the mortgage.[2] In a case where the manu-

[1] Davidson *v.* Westchester Gas Light Co., (1885) 99 N. Y. 558, 563, 564, 565.

[2] Evans *v.* Boston Heating Co., (1892) 157 Mass. 37. *Arguendo* it was said: "The general power of a railroad company, which is undoubtedly a public or a *quasi* public corporation, to make a mortgage of its property, was much discussed by this court in Commonwealth *v.* Smith, 10 Allen, 448. It was there held that such a company, which was created for the sole purpose of constructing, owning and managing a railroad, and authorized to take land under the power of eminent domain, could not make a mortgage in a manner impliedly prohibited by statute; and it was said that there were innumerable objections to such a corporation alienating its franchise and conferring its powers and privileges upon another person or body without authority other than that derived from the fact of its own incorporation. It was also said: 'The power to mortgage can only be coextensive with the power to alienate absolutely, because every mortgage may become an absolute conveyance by foreclosure.' And in Richardson *v.* Sibley, 11 Allen, 65, it was held that under the statute of 1864, chapter 229, section 24, providing that no street railway corporation shall sell or lease its road or property unless authorized so to do by its charter or by special act of the legislature, such a corporation could not mortgage its property." They then said: "The doctrine of these cases does not apply to ordinary trading or manufacturing corporations. Thus, in Treadwell *v.* Salisbury Manuf. Co., 7 Gray, 393, it was held that the directors of a manufacturing corporation might, pursuant to the votes of a majority of its stockholders, though against the protest of the minority, sell the entire property of the corporation to a new corporation. The distinction between such corporations and 'corporations established for objects *quasi* public, such as railway, canal and turnpike corporations to which the right of eminent domain and other large privileges are granted in order to enable them to accommodate the public, was pointed out on page 404 by Mr. Justice Bigelow. And in Commonwealth *v.* Smith it was said by Mr. Justice Hoar: 'The general power to dispose of and alienate its property is also incidental to every corporation not re-

facturing company had executed a mortgage for a large amount to secure a balance of indebtedness due for the purchase price of real estate and for advances made for erecting the buildings of the company, there was a question of whether the paper signed by stockholders, either expressly or by legal intendment, was sufficient to manifest a consent to this mortgage. The paper referred to expressly consented that the company execute to the

stricted in this respect by express legislation or by the purposes for which it is created, and the nature of the duties and liabilities imposed by its charter.' 10 Allen, 455. The policy of the commonwealth in regard to railroads and street railways as set forth in the cases above cited has since been changed. The statute of 1874, chapter 372, section 49, provided: 'Any railroad corporation, by a vote at a meeting called for the purpose, may issue bonds to provide means for funding its floating debt or for the payment of money borrowed for any lawful purpose.' This was amended by the statute of 1875, chapter 58, section 1, by adding the words, 'And may mortgage or pledge as security for the payment of such bonds any part or all of its road, equipment or franchise, or any part or all of its property, real or personal.' These provisions are incorporated in the Public Statutes, chapter 112, section 62. By the statute of 1889, chapter 316, a power is given to a street railway company by a vote of a majority in interest of its stockholders, to authorize the issue of coupon or registered bonds, 'secured by a mortgage of a part or of the whole of the railway of such company and its equipments, franchise and other property, real and personal.' By the statute of 1870, chapter 224, the legislature passed a general law authorizing the formation of various kinds of manufacturing and trading corporations, including in section 5 those for the purpose of making and selling gas for light in a city or town. Section 15 directs how the business of the company shall be managed, and concludes: 'But no conveyance or mortgage of the real estate of the company or lease thereof for more than one year shall be made unless authorized by a vote of the stockholders at a meeting called for the purpose.' By the statute of 1879, chapter 202, section 1, companies were authorized to be formed 'for the purpose of making and selling gas for lights or for the purpose of generating and furnishing steam or hot water for heating, cooking and mechanical power, in any city or town, or for either or both of said purposes,' under the provisions of the statute of 1870, chapter 224. It is from these acts that sections 11 and 23 of Public Statutes, chapter 106, are derived. Without relying upon the remarks of Chief Justice BIGELOW in Commonwealth *v.* Lowell Gas Light Co., 12 Allen, 75, which are strongly in favor of the view that a gas company is not a *quasi* public corporation, it seems to us very clear that the legislature intended to treat a gas company or a heating company as an ordinary manufacturing corporation and not as a *quasi* public corporation so far as the power to make a mortgage is concerned, and that the peculiar language of the statute of 1870, chapter 224, section 15, and of Public Statutes, chapter 106, section 23, is due to the fact that as a manufacturing corporation it could make a mortgage without special authority."

other corporation to which it was indebted as above stated "a bond conditioned for the payment of ———, and a mortgage to secure the same upon the lands and premises by them owned, situate in the city of Brooklyn," etc. The New York Court of Appeals, CHURCH, Ch. J., delivering the opinion, said: "Regarding this as authority from principal to agent, taken in connection with the act of 1864, I think it sufficient to authorize a mortgage to secure any debt of the character specified in the act of 1864 which the manufacturing corporation owed the plaintiff. It is necessary to specify the amount of the debt or the character of it. It is conceded that if the paper had authorized the payment of any debt owing to the plaintiff, it would, in this respect, have been sufficient. The authority was unlimited as to the amount, and, therefore, it authorized securing any amount which the act authorized to be secured. This, it seems to me, is its legal effect, and it is as effectual as if it had specified the indebtedness or referred to the debt as one owing to the plaintiff. No statute authority was requisite to the giving of the bond. The stockholders expressly authorized a bond to be given, and, as the amount was not restricted, I think, upon recognized principles in analogous cases, that the authority was ample to execute the bond in question. The stockholders themselves would not, in the absence of fraud, be heard to deny this authority. It would not, of course, authorize a bond for a sum not owing or for a debt not authorized to be secured by mortgage, but within this limitation it would authorize a bond for any amount." The contention in part of the appellant here was that not only the particular sum be named, but the date and terms of the mortgage must be specified. The chief justice said upon that: "[Such] a construction * * would practically destroy the value of the provision. The defendant could not have been misled. The consent in this case was ample to put him upon inquiry. If he examined the files, he was informed that the stockholders had authorized a mortgage to secure a bond for an amount limited only by the amount of the debt actually existing of a specified nature, and the mortgage on record informed him of the extent to which the authority had been exercised. He seeks to gain a preference, not by objecting either that the amount of the debt or its nature was not correct and legitimate, nor claiming that he was in any manner deceived or misled, but by criticising the form in

which those interested saw fit to express their assent. Assuming his right to object, we think the defects must be so radical that an intention to consent cannot be inferred."[1] The statute of New York, which required the written assent of stockholders owning two-thirds of its capital stock to be first filed to authorize the execution of a mortgage by a corporation as security for debts incurred, has been held by the Court of Appeals to have been complied with where the requisite consent was given, although not filed before the execution of the mortgage and no rights of other creditors had intervened to make the mortgage valid in this respect as against the company and its stockholders.[2] A resolution at a stockholders' meeting, passed by vote of stockholders owning more than two-thirds of the stock, entered on the minutes and attested by the secretary, has been held to be a "written assent" within the meaning of the statute of New York requiring the assent of such a proportion of stockholders to the execution of a mortgage by a corporation.[3] A corporation formed under the act of New York for the formation of manufacturing and other kinds of corporations contested the validity of a mortgage upon the real estate of the corporation made to secure the payment of bonds of some of which the defendants were the holders. The validity of the mortgage was impeached upon the ground that "the written assent of the stockholders owning at least two-thirds of the capital stock" was required by the statute. There was a written assent. The corporation's claim as to this was that eighty shares represented in the assent had never been lawfully issued, and that the remaining shares were not two-thirds of the capital. The judge below in effect found that if the eighty shares were excluded there were still represented in the assent two-thirds of the capital stock. The Superior Court

[1] Greenpoint Sugar Co. *v.* Whitin, (1877) 69 N. Y. 328, 334, 335, 336.

[2] Martin *v.* Niagara Falls Paper Manufacturing Co., (1890) 122 N. Y. 165; s. c., 25 N. E. Rep. 303; citing Rochester Savings Bank *v.* Averell, 96 N. Y. 467.

[3] Beebe *v.* Richmond Light, Heat & Power Co., 35 N. Y. Supp. 1. Assent of stockholders to mortgage: Market & Fulton National Bank *v.* Jones, 7 Misc. Rep. 207; s. c., 27 N. Y. Supp. 677; Adams Cotton Mills *v.* Dimmick, 96 Ala. 238. That the statute of New York of 1890, requiring the mutual assent of two-thirds of the stockholders to the execution of a corporate mortgage, is not applicable to a mortgage given in fulfillment of a valid and obligatory contract made upon a full and valuable consideration before the passage of the statute, see Atlantic Trust Co. *v.* Proceeds of the Vigilancia, 68 Fed. Rep. 781.

of New York city in General Term affirmed the finding and judgment.[1] The assent to a mortgage executed in a case by a manufacturing corporation of the state of New York was signed by a certain number of stockholders and by the corporation itself, by its secretary and president, this being done as they intended to represent 940 of the 5,000 total shares which stood in the name of the corporation itself. The New York Court of Appeals held that these shares represented by the company could not be counted to make the amount in value required by the statutes of the state to assent to the execution of a mortgage.[2]

[1] Lyceum *v.* Ellis, (1890) 57 N. Y. Super. Ct. 532; s. c., 8 N. Y. Supp. 867. "In this [finding]," said SEDGWICK, Ch. J., in General Term of the Superior Court of New York city, speaking for a majority of the court, "he was correct, under the case of Greenpoint Sugar Co. *v.* Whitin, 69 N. Y. 328. That case decided that 'for the purposes of this act * * * the amount actually issued and owned should be regarded as the amount of the capital stock. The design was to confer this power of assent upon those who represented two-thirds of the actual stock. They represented two-thirds of the pecuniary interest and property of the corporation. The learned counsel for the plaintiff argues that the case cited makes a limitation of the general principle announced by saying in reference to what it held to the amount of the capital stock or the two thousand shares, 'and, for aught that appears, no more was intended to be issued.' The meaning of this, I take to be, that an assent to a mortgage made by two-thirds of the then capital stock, will not be sufficient, if, also, then there is a definite intention of increasing the actual stock by future issuing of shares in a manner that will increase the actual stock. The intention referred to is not a general intention; that is presumed as to all shares not transferred. It would be an attempt to evade the statute, that a mortgage should be made upon the assent of two-thirds of the actual capital, when that was accomplished by the beginning of an arrangement to increase the capital, or even by an intention forthwith to make such an arrangement. That method would be fraudulent as to those who might afterwards become the owners of shares. In the present case the fact is that if there were an intention to issue the shares one hundred and twenty in number, of which the eighty was represented in the assent, the result would be that those one hundred and twenty shares must be considered part of the actual capital, and then the persons to whom the issue was made would be considered the owners of the shares. In such case there was an assent of two-thirds of the capital stock upon the position taken by the plaintiff.'"

[2] Vail *v.* Hamilton, (1881) 85 N. Y. 453, 456, 457. DANFORTH, J., said: "The persons who became 'a body politic and corporate' under the name of the 'Secor Sewing Machine Company,' were made capable of buying, purchasing, holding and conveying in their corporate name any lands, goods, wares and merchandise necessary to enable the company to carry on the operations named in their certificate of incorporation. But while a certain limited number of the stockholders, to be called trustees, were empowered in that character to manage this property

The Supreme Court of New York in General Term, where it was part of the arrangement under which land was conveyed to an incorporated association that it should give two mortgages to secure future advances for improvements thereon, and the mortgages and the deed were executed and delivered contemporaneously, sustained the finding of a referee that the mortgages were not invalid because of any failure to comply with the requirements of a statute of that state, providing that associations incorporated under it shall, as a condition precedent to the giving of a mortgage to secure a debt contracted by it in the course of its business, have the assent of two-thirds of the owners of the capital stock, holding these mortgages not within the act.[1] In a West Virginia case, a corporation of the state of New York, in an action to foreclose a mortgage upon its mining lands in the former state, the corporation attempted to put in issue the validity of the mortgage, claiming that it was invalid by reason of the assent of stockholders required under the New York statutes not having been given. Even if this were conceded, the Court

and the stock and concerns of the company, neither in a corporate capacity, nor through its trustees, was it permitted to mortgage the same without first obtaining and filing 'the written assent of the stockholders owning at least two-thirds of the capital stock of such' company. [Citing the laws of the state.] It is noticeable that there is thus called into action the corporation as an artificial entity, the body of the trustees as its agents, and, lastly, the constituent members of the corporation or the several individuals composing it. To each of these a duty is assigned, and, to make valid the transaction now before us, it is plain that something more than corporate action was required. The corporation might become a party to the mortgage, and the trustees direct its officers to execute it; but there must still be the assent of the stockholder. The will of the whole body, expressed by vote or resolution, cannot take its place. The name of the corporation is signed to the assent. This, if it amounts to anything, must be the result of corporate, not individual action. It was signed by its officers, and their act, to bind even the corporation, must have been official; it can have no force as representing an individual. As to nine hundred and forty shares, therefore, there is no other assent to the mortgage in question than that of the corporation. The mortgage itself must be deemed a corporate act, and assent thereto by the same body can give it no additional validity. As to those shares assent has not been given. It follows, also, that as the corporation cannot assent for the stockholders, neither can one stockholder for another; nor can one who assents on the strength of stock standing in his own name, be deemed to represent a proportionate amount of the stock owned by the corporation."

[1] McComb *v.* Barcelona Apartment Assn., (1890) 10 N. Y. Supp. 546; citing Sugar Co. *v.* Whitin, 69 N. Y. 328, 336, 337; Coman *v.* Lakey, 80 N. Y. 345.

of Appeals of West Virginia held that the question of whether the proper assent of stockholders had been given could not be raised by the corporation.[1] The validity of a mortgage executed by a corporation in North Carolina was assailed by other creditors, and the Supreme Court of that state made the following rulings: The assent of a majority of stockholders, expressed elsewhere than at a meeting of the stockholders, as where the assent of each is given separately and at different times to a person who goes around to them privately, does not bind the company. An agency to execute a mortgage given in this manner gives no validity to the mortgage. It is not the corporation's act, which can only be authorized in the mode required by law. The use by the company of money raised by such mortgage would not of itself be a ratification. If the company ratify the mortgage, it would not validate it as to other creditors if the mortgage is invalid when registered.[2]

§ 508. Mortgages and trust deeds — rules as to place of execution, authorization, mode of execution, to whom executed, record, etc.— The United States Circuit Court for the eastern district of Louisiana held, in a suit to foreclose a mort-

[1] Boyce *v.* Montauk Gas Coal Co., (W. Va. 1892) 16 S. E. Rep. 501. The court said: "In the case of Beecher *v.* Rolling Mill Co., 45 Mich. 103; s. c., 7 N. W. Rep. 695, under a statute which forbade a manufacturing company to mortgage its property unless authorized thereto by vote of stockholders holding three-fifths interest, and notified of the object of the meeting called to obtain such vote, and which provides that without notice the proceedings shall not be valid. where notice was given of a meeting to authorize the issue of bonds to the extent of one hundred thousand dollars, secured by mortgage, and the meeting actually authorized an issue to the amount of one hundred and fifty thousand dollars, it was held that, so long as the corporation raised no objection to the proceedings no one else could. Judge Cooley, delivering the opinion of the court, says: 'The statute now under consideration was passed to protect the interests of stockholders in mining companies. It intends that their mining property shall not be conveyed away or mortgaged except by their deliberate action, after they have been notified of a proposal to do so, and have had time to deliberate upon and fully consider it. But the matter does not concern the public at large. No principle of public policy is at stake. No wrong, direct or indirect, is done to any human being, if conveyance is made or mortgage given without the exact notice required, unless it be a wrong to the stockholders themselves; and, as others are not concerned, why should the statute give them the right to raise questions of regularity which the stockholders elect to waive? We are satisfied such was not its purpose.'"

[2] Duke *v.* Markham, (1890) 105 N. C. 131; s. c., 10 S. E. Rep. 1017.

gage given by a New Jersey corporation upon its property in Louisiana, that it was no defense that at the time of executing the mortgage some of the directors were not residents of New Jersey.[1] Neither was the mortgage invalidated by the fact that the directors went into New Jersey and remained there only a brief period, to hold the meeting at which was passed the resolution authorizing the mortgage.[2] A trust deed to secure bonds will not be held invalid because it may not be in strict accordance in some particulars with the resolution of the corporation's board of directors authorizing it, when, subsequent to its execution, the board of directors have recognized the existence and validity of the mortgage by directing the issuance of the amount of bonds it was given to secure.[3] Certain officers and directors of a private corporation in Nebraska loaned their credit to it by executing notes for the accommodation of the corporation, thus obtaining capital for its operations. They were secured by a mortgage upon the plant. When they brought action to foreclose this mortgage certain alleged stockholders intervened and defended upon various grounds, with a prayer for a dismissal of the petition, and that the mortgages and the record thereof be canceled, and for equitable relief. These interveners, by an amendment of their answer, with the permission of the court, also claimed to be creditors of the corporation for advances made to it, and prayed for a receiver to take charge of its property, convert it into cash, and apply the proceeds to the payment of its general indebtedness, and if anything was left to apply it *pro rata* among the stockholders. There was a finding and a decree of foreclosure in favor of the plaintiffs, and an appeal by the interveners. The first proposition argued before the Supreme Court was that the evidence failed to show authority from the board of directors for the execution of the mortgages, or either

[1] Wheelwright *v.* St. Louis, N. O. & O. Canal Transportation Co., (1893) 56 Fed. Rep. 164. BILLINGS, D. J., said: Whatever force there might have been in this objection in case the state had brought a *quo warranto* against the corporation, there is no force in it in this proceeding. The board was elected by stockholders in the manner pointed out by the charter, and as against a creditor the directors are clearly competent.

[2] Wheelwright *v.* St. Louis, N. O. & O. Canal Transportation Co., (1893) 56 Fed. Rep. 164. As to officers acting outside the state, see Missouri Lead Mine & Smelting Co. *v.* Reinhard, 114 Mo. 218.

[3] First Nat. Bank *v.* Sioux City Terminal R. R. & Warehouse Co., 69 Fed. Rep. 441.

of them. To this argument the court said: "Both mortgages purport to have been executed by the [corporation] and acknowledged in behalf of said [corporation] by F. R. Guthman, president, and E. B. Lewis, secretary, and attested by the seal thereof. The genuineness of the signatures to the mortgage, as well as the official character of the signers, is specifically admitted, but we understand counsel for interveners to contend that authority for the execution of the mortgages must affirmatively appear from the record of the board of directors. To that proposition we cannot give our assent. The signatures of the officers, with the corporate seal attached, is *prima facie* evidence that the mortgages were executed by authority of the company, and the burden of proving want of authority is upon the interveners."[1] Upon the questions raised as to the execution of chattel mortgages of an insolvent Michigan corporation, the United States Circuit Court of Appeals for the sixth circuit held that under the resolution adopted by the directors of the corporation, reciting an agreement by a creditor to advance to the corporation $3,000, and a further sum of $1,000, if required, and authorizing the secretary and treasurer to secure the total indebtedness by chattel mortgage, this creditor, having advanced the $3,000 — the additional $1,000 not being required by the corporation — was entitled to the mortgage. And the further authorization in the resolution of the secretary and treasurer, to secure "any and all other creditors" by subsequent mortgages, did not require a mortgage to secure all other creditors, the word "and," in the opinion of the court, in that connection having the meaning of "or." Neither were the mortgages invalidated by the fact that some of the directors and stockholders who, as such, voted for the resolution authorizing the mortgages, were also guarantors and indorsers upon most of the secured notes.[2] After holding that a heating

[1] Gorder *v.* Plattsmouth Canning Co., (1893) 36 Neb. 548, 551, 552; citing Ang. & Ames Corp. § 217; Boone Corp. § 50; Blackshire *v.* Iowa Homestead Co., 39 Iowa, 624; Whitney *v.* Union Trust Co., 65 N. Y. 577; Davis *v.* Jenney, 1 Met. 221; Williamsburg City Fire Ins. Co. *v.* Frothingham, 122 Mass. 391; Murphy *v.* Welch, 128 Mass. 489; Hamilton *v.* McLaughlin, (Mass.) 12 N. E. Rep. 424; Morris *v.* Keil, 20 Minn. 531; Musser *v.* Johnson, 42 Mo. 74.

[2] Brown *v.* Grand Rapids Parlor Furniture Co., (1893) 58 Fed. Rep. 286, following on this last point, Bank of Montreal *v.* J. E. Potts' Salt & Lumber Co., 90 Mich. 345; s. c., 51 N. W. Rep. 512; citing Hills *v.* Furniture Co., 23 Fed. Rep. 432; County Court *v.* Baltimore & O. R. Co., 35 Fed. Rep. 161, and reviewing many other cases.

company organized under the Public Statutes of Massachusetts (Chap. 106, §§ 11, 23), had authority to make a mortgage to secure bonds issued by it, the Supreme Judicial Court considered the question whether the mortgage was authorized "at a meeting called for the purpose as required by § 23, above referred to." They said: "The notice of the meeting stated the object to be 'to consider the question of an issue of bonds of the company secured by a mortgage of its property.'" There was an objection that the notice did not indicate that final action was to be taken, and, therefore, the action at the meeting did not operate to authorize the execution of the mortgage. The court held that action at the meeting upon the subject of executing this mortgage was properly taken, the notice being sufficiently explicit to amount to a compliance with the statute.[1] The Iowa Supreme Court has held that where the resolution authorizing the execution of a deed of trust conveying the property of a corporation was passed at a meeting of the directors, at which four out of five were shown by the minutes to be present, and the minutes showed that two of them voted for the resolution, and that one of them voted against it, and that it was adopted, but the president, whose vote was not shown by the minutes, signed and approved them, the president will be presumed to have voted for it, and that it

[1] Evans *v.* Boston Heating Co., (1892) 157 Mass. 37. The court said: "The object of a call is undoubtedly to give notice of the business which is to be transacted at the meeting. The notice in this case was issued to members of a business corporation, and it could hardly have been understood by them as calling a meeting simply for the purpose of debate, and we are of opinion that this is not its fair intendment, and that action under it might be taken. At the time of the notice the corporation had a leasehold estate in a parcel of land, with an option to purchase it. We see no reason why this was not 'property' within the meaning of the notice, nor why it was not sufficiently indicated by the notice. After the directors had been authorized at the meeting to purchase the land in which the corporation then had a leasehold estate, and to mortgage 'any or all of the rights, estate, property and franchises' of the corporation, the land was conveyed to the corporation, the property was mortgaged, and the land was paid for out of the proceeds of the mortgage. We do not think that the fact that between the time of the meeting and that of the execution of the mortgage the interest of the corporation in the land changed from an estate for years to a freehold estate made it necessary to call a new meeting or to pass a new vote. The notice of the meeting gave warning that a mortgage of the property of the company was to be considered. The votes passed at the meeting, by fair intendment, contemplated and authorized the doing of what was in fact done."

must be regarded as duly adopted.[1] A number of questions arose in a Massachusetts case as to the powers of the officers of a New Hampshire corporation doing business in the State of Massachusetts, in connection with the execution of a mortgage upon real estate in the latter state. The Supreme Court held, upon the contention that the mortgage made to the savings bank by the corporation was without lawful authority and void, by virtue of the statute of Massachusetts, which provides that no conveyance or mortgage of the real estate of a corporation or "lien thereof for more than one year shall be made, unless authorized by a vote of the stockholders at a meeting called for the purpose," no such vote having been passed authorizing the mortgage in question, that the statute did not refer to foreign corporations.[2] The Iowa

[1] Rollins *v.* Shaver Wagon & Carriage Co., (1890) 80 Iowa, 380; s. c., 45 N. W. Rep. 1037. See as to authority of officers to execute a mortgage, Jesup *v.* City Bank of Racine, 14 Wis. 331; Haven *v.* Adams, 4 Allen, 80; Kennebec & Portland R. R. Co. *v.* Portland & Kennebec R. R. Co., 59 Me. 9; Luse *v.* Isthmus Transit Ry. Co., 6 Or. 125; Miller *v.* Rutland & Washington R. R. Co., 36 Vt. 452; Fitch *v.* Lewiston Steam Mill Co., 80 Me. 34; s. c., 12 Atl. Rep. 732.

[2] Saltmarsh *v.* Spaulding, (1888) 147 Mass. 224; s. c., 17 N. E. Rep. 316. DEVENS, J., speaking for the court, said: "While the general principle undoubtedly is, that the law of the place where real property is situate exclusively governs as to the title of parties therein, the disposition and mode of transfer thereof, and the solemnities attending such transfer, and while we do not doubt that it would be possible to provide by legislation that foreign corporations, permitted to own real property situate in this state, should only transfer the same by the authority of the stockholders, no such provision has been made. Attorney-General *v.* Bay State Mining Co., 99 Mass. 148. While they must comply in their forms of conveyance with those here required, they derive their authority to make them from the rules imposed upon them by the states where they are created." To the further contention that there was no power vested in the board of directors by the laws of New Hampshire which authorized them to make a deed of real estate, the court said: "The by-laws of the corporation vested the management and control of its business and the authority to appoint all necessary agents therefor in the board of directors. The mortgage deed was made in the name of the corporation, and under its seal by the president and treasurer of the corporation, by virtue of an express vote of the directors giving them authority. The General Statutes of New Hampshire of 1878, chapter 147, section 4, clause 3, which are made a part of the case, empowered the corporation to adopt by-laws 'to regulate the number of officers, their powers and duties, the mode of choosing them, and their tenure of office; and any others necessary and suitable to promote the objects of the corporation; and alter and amend the same.' The corporation was one authorized to make contracts necessary and proper for its business, and to purchase, hold and convey real and

Supreme Court has held that a trust deed made by a corporation to secure preferred creditors could not be assailed, as to one of the creditors secured, on the ground that one of the directors who voted for it was her husband and another her brother, and that without their votes it could not have been made.[1] Where a charter of a Pennsylvania corporation provided that the property of the association should be purchased, held, managed and sold by a board of five trustees, a mortgage executed by the president and secretary of the corporation, and not by its trustees, and not sealed with the corporate seal, and there was not to be found on the books of the corporation any resolution authorizing, ratifying, or in any manner recognizing, the making of this mortgage, was held by the Supreme Court of Pennsylvania not to be the act and deed of the corporation, or binding upon it as such.[2] A corporate mortgage has been held valid as against an attack of creditors who were not stockholders, though not authorized by a majority of the stockholders at a "regular general meeting" as required by its charter.[3] No one but a stockholder can take advantage of a failure to advertise a notice of a stockholders' meeting, as required by the Tennessee statute, at which

personal estate necessary for the transaction of its business. Gen. Sts. of N. H. of 1878, chap. 147, §§ 5, 6. The directors, by virtue of the powers implied from their position, had the general control and management of the business, which of necessity involved the raising of money to carry it on. It is found that the money raised by means of the mortgage was expended in the real estate of the mortgagor. In the absence of any prohibitory statute, a sufficient authority is shown on the part of the directors to mortgage the property, and doing so they could adopt the form ordinarily in use where the real estate was situated." Citing Burrill *v.* Nahant Bank, 2 Met. 163, 166; Sargent *v.* Webster, 13 Met. 497; Hendee *v.* Pinkerton, 14 Allen, 381, 387; Despatch Line of Packets *v.* Bellamy Mfg. Co., 12 N. H. 205.

[1] Rollins *v.* Shaver Wagon & Carriage Co., (1890) 80 Iowa, 380; s. c., 45 N. W. Rep. 1037. The court said: "She was not an officer nor stockholder of the company at that time; but, had she been one of its officers, that fact would not have deprived her of the right to enter into competition with other creditors in a race of diligence, availing herself of her superior knowledge and of her position to obtain security for or payment of her debt. Buell *v.* Buckingham, 16 Iowa, 291; Warfield *v.* Canning Co., 72 Iowa, 666; Garrett *v.* Plow Co., 70 Iowa, 697. Much less would it have prevented her relatives on the board from acting in good faith, and without fraudulent intent, to secure or pay her."

[2] McElroy *v.* Nucleus Association, (1890) 131 Pa. St. 393; s. c., 18 Atl. Rep. 1063; 25 W. N. C. 262.

[3] Antietam Paper Co. *v.* Chronicle Pub. Co., (N. C.) 20 S. E. Rep. 366.

a mortgage of a railroad is authorized.[1] A mortgage having been executed under the seal of a corporation, regular on its face, and by the properly constituted officers, is *prima facie* evidence that the corporation authorized its execution, and those objecting to it have the burden of proving that it was executed without such authority.[13] It has been held by the United States Circuit

[1] Central Trust Co. *v.* Condon, 67 Fed. Rep. 84. As to authority to execute mortgages to secure bonds or other obligations, see Adams Cotton Mills *v.* Dimmick, 96 Ala. 238; Brown *v.* Supply Co., 23 Or. 541; Grant *v.* Railroad Co., 13 U. S. App. 1; s. c., 4 C. C. A. 511; Manhattan Hardware Co. *v.* Phalen, (Pa.) 18 Atl. Rep. 428; Wright *v.* Hughes, 119 Ind. 324; s. c., 21 N. E. Rep. 907. When a mortgage is void for non-compliance with the statute in its execution, see Alta Silver Mining Co. *v.* Alta Placer Mining Co., 78 Cal. 629; s. c., 21 Pac. Rep. 373.

[13] Wood *v.* Whelen, 93 Ill. 153. In Saltmarsh *v.* Spaulding, (1888) 147 Mass. 224; s. c., 17 N. E. Rep. 316, as to the execution of mortgages by a corporation, it was said: "The provision that a corporation authorized to hold real estate may convey the same by an agent duly appointed for that purpose (Gen. Sts. of N. H. of 1878, chap. 135, § 2) does not exclude other modes of conveyance; as, for instance, in the name and under the seal of the corporation itself, and by the president and treasurer. Especially would this be so where the latter form is that used where the real estate is situated. Morris *v.* Keil, 20 Minn. 531; Bason *v.* King's Mining Co., 90 N. C. 417. It is said, however, that, even if the directors might make the mortgage, they had no power to delegate this authority, but must exercise it themselves. The directors delegated no discretionary power; they determined upon the mortgage, and made the president and treasurer simply the agents to execute formally that which they themselves had voted to do. In Burrill *v.* Nahant Bank, 2 Met. 163, it was accordingly held that the directors of the bank not only might mortgage its real estate to secure a debt due from the bank, but might delegate such authority to a committee of their own number." There was a further contention that a vote of the directors passed without the state to which their corporation owed its existence was void. Upon this the court said: "The corporation was organized for the purpose of doing business without the limits of New Hampshire. Its works were within this state, and here its contracts were made and its business was conducted. Its by-laws, passed at a meeting of the corporation in New Hampshire, while they provide for the annual meeting of the corporation in that state, and for the choice of officers there, provide also for meetings of the directors for business in this state, for the control of the business and the appointment of the necessary agents here, and for the filling here by the directors temporarily of any vacancies that may have occurred. We do not doubt that this may be done by the corporation. It would certainly be an extraordinary anomaly, if, while by the comity prevailing between the states the corporation was allowed to conduct its business, it could disavow the acts of those whom it has appointed to direct its business here, on the ground that the votes by which they were done were passed here. The case cited, of Miller *v.* Ewer, 27 Me. 509, to sustain the statement in Angell & Ames on

Court of Appeals for the fifth circuit that when an assistant secretary of a railroad company acted as the secretary in fact, transacting the business of the company with the knowledge of the directors, and as such *de facto* secretary attached the seal of the company to mortgages executed by the company on land granted to it by the state of Florida, it was not necessary for the mortgagee, in establishing the validity of the mortgages, to show that he was assistant secretary *de jure*.[1] The statute of Montana, requiring foreign corporations, before doing business in the state, to file, in the office of the recorder of the county wherein it intended to carry on business, a copy of its charter and certain verified statements as to its capital, has been held in the United States Circuit Court for the district of Montana not to prevent a foreign trust company which has not complied therewith from purchasing securities of a railroad company in the state and taking a mortgage upon its property to secure them.[2] There having been an objection to an answer in this case that a trust company holding a mortgage upon railroad securities which had filed a cross bill asking for relief was not entitled to it for failure to record its mortgage as required by the statute of Montana as to the recording of chattel mortgages, the objection was sustained in the federal court, the court holding that in this matter the statute relating to mortgages by railroad companies, providing that the record in the office of the secretary of state of a mortgage by a

American Corporations, § 274, on which the defendants rely, only holds that a corporation established under a charter of the state of Maine could not organize in another state, and that the attempt to do so was void, but recognizes fully that a corporation only organized, and acting within the limits of the state granting the charter, may, by agents duly constituted, act and contract without the limits of the state."

[1] Augusta, Tallahassee & Gulf R. Co. *v.* Kittel, (1892) 52 Fed. Rep. 63.

[2] Gilchrist *v.* Helena, H. S. & S. R. Co., (1891) 47 Fed. Rep. 593. KNOWLES, J., said: "I do not think the purchasing of securities or the accepting of a mortgage upon property from a company in Montana can be considered as doing business in Montana." See Manufacturing Co. *v.* Ferguson, 113 U. S. 727; s. c., 5 Sup. Ct. Rep. 739. The Indiana statute, which declares conveyances in trust to other than *bona fide* residents of the state invalid, has been held not to apply to deeds of trust to a foreign corporation, securing the bonds of a railroad corporation within that state, in Farmers' Loan & Trust Co. *v.* Chicago & Atlantic Ry. Co., 27 Fed. Rep. 146. A mortgage upon railroad property, executed to a foreign corporation as trustee in Illinois to secure payment of bonds payable outside the state has also been held not to be prohibited by the laws of that state or contrary to public policy, in Hervey *v.* Illinois Midland Ry. Co., 28 Fed. Rep. 169.

railroad company, the line of which is wholly or in part in Montana, shall be notice to all parties without further record, was not repealed by implication by the passage of the statute as to chattel mortgages, and its having been complied with, was sufficient record of the mortgage.[1] As a mortgage of railroad rolling stock is a chattel mortgage under Civil Code of California, section 2956, it is void against a subsequent attachment, when not executed and recorded in the manner prescribed, or accompanied by the affidavits of good faith required by section 2957.[2] When a mortgage by a corporation is signed by the president, secretary and two stockholders and duly witnessed, but there is no common seal attached, and the probate recites that it is "acknowledged by the secretary, who also proves the execution by the president and two stockholders," such probate is insufficient and does not authorize registration and is ineffectual to pass title as against creditors.[3]

§ 509. **Estoppel of corporation to deny authority of officers to mortgage.**— A corporation in the state of Washington had given its notes and executed a mortgage upon its property to secure the payment of these notes. The note and mortgate were executed and delivered by the president and secretary of the corporation without being previously authorized by the board of trustees so to do. Upon the holder of the mortgage proceeding to foreclose his mortgage the corporation defended upon the ground that the note and mortgage were executed by its executive officers without authority. The Supreme Court of that state held that although the note and mortgage may have been executed without authority from its board of trustees, yet the corporation would be estopped from denying the authority of its officers where it appeared that the corporation was aware of the transaction from the first and never objected or sought to repudiate it; that at a regular meeting of its board of trustees the payment of the note and mortgage was considered and discussed, and

[1] Gilchrist *v.* Helena, H. S. & S. R. Co., (1891) 47 Fed. Rep. 593.

[2] Union Loan & Trust Co. *v.* Southern California Motor Road Co., (1892) 51 Fed. Rep. 840. As to recording such mortgages, see Allen *v.* Montgomery R. R. Co., 11 Ala. 437; Bement *v.* Plattsburgh & Montreal R. R. Co., 47 Barb. 104; Coe *v.* Col., Piqua & Ind. R. R. Co., 10 Ohio St. 372; Branch Sons & Co. *v.* Atlantic & Gulf R. R. Co., 3 Woods, 481.

[3] Duke *v.* Markham, (1890) 105 N. C. 131; s. c., 10 S. E. Rep. 1017.

in fact two payments made thereon out of the corporate funds; and that no act of repudiation was undertaken until two years after the execution of the note and mortgage, and after they had passed into the hands of innocent purchasers.[1] In this case it was claimed, further, that if the debt were valid, the mortgage given to secure it was not, on account of an alleged absence of a resolution by the directors empowering the president of the corporation to make the mortgage. Of this it was said, in the opinion rendered by the Supreme Court: "But the mortgage recited such a resolution, and it is not denied that it is contained in the minutes of the corporation. The mortgage is under the corporate seal, signed by the president and attested by the secretary of the [corporation]. The mortgagee knew that the corporation had power to borrow money upon bond and mortgage, and in the utmost good faith advanced his money to the corporation and accepted the mortgage as security for it. Upon its face the mortgage represented that it was duly authorized by the directors, and under the circumstances he was not bound to look beyond it. He had the right to assume as against the company that all matters of internal management had been complied with. The minutes of the corporation were not for his inspection, and, if he had been allowed access to them, would have sustained the recital in the mortgage. No director or stockholder has ever claimed that the mortgage was unauthorized, but, on the contrary, stockholders owning a clear majority of the stock issued by the corporation have recognized its validity in their bill for the appointment of a receiver. It is the receiver appointed upon their bill who is

[1] Seal *v.* Puget Sound Loan & Investment Co., (1892) 5 Wash. St. 422. The Supreme Court of Judicature of Maine, in Fitch *v.* Lewiston Steam Mill Co., 80 Me. 34; s. c., 12 Atl. Rep. 732, held similarly. Referring to the facts in this particular case, it was said: "Here was the express authority of the corporation created and existing by vote duly recorded, authorizing and empowering its treasurer to make, sell, execute and deliver, in the name of the corporation, any and all conveyances of land by deed, bond, or otherwise. This authority was broad enough to embrace the transaction in relation to this mortgage. The treasurer, not only in this case, but on other occasions, had acted in like manner, relying on the authority conferred by this vote. The party who advanced the money and received the mortgage was led to believe that the treasurer was acting under that authority. This is not denied. Consequently, after enjoying the benefit of the loan, and acquiescing in the transaction for more than eight years, it does not lie in the mouth of the defendant corporation to say that the mortgage is inoperative and void. Aurora Agr. & Hort. Society *v.* Paddock, 80 Ill. 263."

now seeking, against their protest, to destroy it. For aught that appears in his affidavit of defense, every director and stockholder of the company knew of the loan and mortgage and ratified both by acquiescence. As neither the corporation, its stockholders, nor its creditors can now allege a want of authority to make the loan and mortgage, the receiver cannot do so for them."[1]

§ 510. Effect of laches of corporation in repudiating a mortgage.— Where the president of a company chartered for the purpose of constructing a railroad, under authorization of the board of directors, mortgages the company's land granted to it by a state, and the money, which is loaned in good faith, is used by the officers of the company for company purposes, and the validity of the transaction is recognized by payment of interest, and the transaction being brought to the notice of the directors, both actually and by its being recorded, and there being no repudiation of the mortgage or denial of the authority of the president in the premises, a subsequent resolution by part of the directors, made long afterwards, disaffirming and annulling the president's authority, will not invalidate the transaction or prevent a foreclosure, as by not promptly disaffirming the transaction the company would tacitly ratify the act of the president.[2]

§ 511. What are reasonable provisions in a mortgage.— A trustee of a railroad mortgage brought his action for foreclosure. The holder of bonds secured by several prior mortgages intervened in the suit and asked the foreclosure of these prior mortgages in this action. There were demurrers by various trust companies, trustees in different mortgages, to his complaint in intervention that it did not show a ground for intervention, or state facts sufficient to constitute a cause of action. The inter-

[1] Manhattan Hardware Co. *v.* Phalen, (1889) 128 Pa. St. 110, 118, 119. See, for a ruling upon a similar mortgage by this manufacturing corporation, Manhattan Hardware Co. *v.* Roland, (1889) 128 Pa. St. 119. As to estoppel of the corporation in such a case, see Brooke *v.* Railroad Co., 108 Pa. St. 529; Chestnut Hill, etc., Co. *v.* Ratter, 4 S. & R. 6; Bank of Kentucky *v.* Schuylkill Bank, 1 Pars. 251; Hackensack Water Co. *v.* De Kay, 36 N. J. Eq. 548; Willis *v.* Phila., etc., R. Co., 6 W. N. C. 461; Oil Creek, etc., R. Co. *v.* Penna. Trans. Co., 83 Pa. St. 160; Wright *v.* Pipe Line Co., 101 Pa. St. 204; Penn. N. Gas Co. *v.* Cook, 123 Pa. St. 170.

[2] Augusta, Tallahassee & Gulf R. Co. *v.* Kittel, (1892) 52 Fed. Rep. 63.

vener claimed that the provisions of the mortgage were void in so far as they attempted to deprive the holder of any of the bonds which may have become due by default in payment of the interest coupons or the holders of any of the past due coupons from enforcing the remedy whereby he might have his lien established upon the mortgaged property without the requisition of the holders of not less than twenty-five *per centum* of the said bonds then outstanding; that the provisions were in fact an attempt to oust the jurisdiction of any court to entertain a complaint by, or give relief to, the holders of less than twenty-five *per centum* of the outstanding bonds. The Supreme Court of Minnesota, upon the question raised by this contention, held that such provisions were reasonable and valid.[1]

[1] Seibert *v.* Minneapolis & St. Louis Ry. Co. (Griggs, Intervener), (1893) 52 Minn. 148; s. c., 53 N. W. Rep. 1134. It was said by the court: "We are unable to see why the bondholders, subject to reasonable limitations, may not be bound by stipulations in the mortgage of this character, waiving a default, and providing, subject to the conditions named, for the foreclosure by the trustees exclusively. The interests of the bondholders as a class and the nature of the security are to be considered. They are agreements which the bondholders are at liberty to make, and there is nothing illegal or contrary to public policy in them. Chicago & V. R. Co. *v.* Fosdick, 106 U. S. 47, 77; s. c., 1 Sup. Ct. Rep. 10. Each bondholder enters into contract relations with each and all of his co-bondholders. His right to appropriate the security in satisfaction of his bond in such lawful manner as he may choose is modified not only by the express provisions of the mortgage, but by the peculiar nature of the security. Gates *v.* Railroad Co., 53 Conn. 346; s. c., 5 Atl. Rep. 695; Shaw *v.* Railroad Co., 100 U. S. 605, 612; Canada Southern R. Co. *v.* Gebhard, 109 U. S. 534–537; s. c., 3 Sup. Ct. Rep. 363; Guilford *v.* Minneapolis, S. Ste. M. & A. Ry. Co,, 48 Minn. 560; s. c., 51 N. W. Rep. 658. The legislature would have had an undoubted right to have incorporated in the enabling statute authorizing the execution of the mortgage and the issuance of the bonds secured thereby, a provision requiring the mortgage to contain similar stipulations. Howell *v.* Western Railroad Co., 94 U. S. 463–466. It is clear then that it would be competent for the bondholders themselves to agree to them. They are to be treated as *stricti juris*, but, nevertheless, are to be reasonably construed in view of the nature of the mortgage, which is the common security for all the bondholders, and the purposes to be subserved in making them. There is no doubt that the parties could lawfully provide in the same instrument for a reasonable extension of the time for the commencement of foreclosure proceedings, to be determined at the option of a majority of the bondholders. * * * Why may not the mortgage in the common interest stipulate the conditions under which this right may be exercised by the bondholders, and, in order to avoid the risk of rash or arbitrary proceedings, which might result in great in-

§ 512. **Chattel mortgages of corporations.**— It was claimed before the United States Circuit Court of Appeals for the sixth circuit that the chattel mortgages executed by the insolvent corporation, to set aside which this bill in equity was originally brought, were violative of certain statutes of the state of Michigan, the domicile of the corporation. The court held that these chattel mortgages executed by the insolvent corporation to secure a portion of its debts were not common-law assignments with preferences, as between creditors, within 2 Howell's Statutes of Michigan, section 8739, declaring such assignments void.[1] Neither was a chattel mortgage an assignment within the statute, although, in view of the impossibility that the corporation can ever redeem, the effect of the mortgage necessarily is to transfer the property to the trustee named in the mortgage, who thereunder may sell and distribute the proceeds in the same manner as an assignee under such an assignment, as the right of redemption by the corporation or attaching creditors would, nevertheless, exist.[2] The defeasance clause in these mortgages, providing that, if the debts be paid at maturity, the mortgage and the notes secured thereby shall be void, and containing an agreement to pay the same accordingly, was held not to be rendered nugatory by the fact that one of the notes secured was due when the mortgage was made, and that it should rather be construed to require a demand for payment of the note subsequent to the giving of the mortgage, and a refusal to pay before the mortgage would become

jury to the security, provide that no such proceedings should be instituted by an individual bondholder except upon the refusal of the trustee to obey the requisition of a reasonable number of bondholders. It is not the intention or effect of such conditions or stipulations to divest the bondholders of their right to judicial remedies, or to oust the courts of their jurisdiction; it is merely the imposition of certain conditions upon themselves in respect to the exercise of that right." Provisions in a mortgage which do not make it void: Vincent *v.* Snoqualmie Mill Co., 7 Wash. 566; s. c., 35 Pac. Rep. 396. Mortgages given without authority: Ohio Val. Nat. Bank *v.* Walton Architectural Iron Co., 30 Wkly. Law Bull. 382; Currie *v.* Bowman, (Or.) 35 Pac. Rep. 848; Wright *v.* First National Bank, (N. J. Eq.) 28 Atl. Rep. 719.

[1] Brown *v.* Grand Rapids Parlor Furniture Co., (1893) 58 Fed. Rep. 286, following Sheldon *v.* Mann, 85 Mich. 265; s. c., 48 N. W. Rep. 573; Warner *v.* Littlefield, 89 Mich. 329; s. c., 50 N. W. Rep. 721; Bank of Montreal *v.* J. E. Potts Salt & Lumber Co., 90 Mich. 345; s. c., 51 N. W. Rep. 512.

[2] Brown *v.* Grand Rapids Parlor Furniture Co., (1893) 58 Fed. Rep. 286; Warner *v.* Littlefield, 89 Mich. 329; s. c., 50 N. W. Rep. 721, distinguished.

absolute.[1] In one of the special courts of the city of New York, a complaint of the purchasers of the personal property of a printing company at a sale, with notice of certain chattel mortgages, seeking equitable relief against the holders of these mortgages, that the latter be declared to be void, and for an injunction, was dismissed. The court in General Term affirmed the dismissal of the suit. In the opinion rendered, it is stated that "the plaintiff claimed in its complaint that the chattel mortgages were invalid because the consent of the corporation had not been obtained for the execution thereof. The defendants contend (1) that as the plaintiff represented the purchasers of these chattels, who had notice of the execution of the mortgages before the sales, it is estopped from taking advantage of such a defect, if it existed; (2) that, in fact, the written consent of the corporation to the execution of the mortgages had been obtained and was duly filed. The plaintiff next contends that, as to one of the printing presses, it had been substituted, after the first mortgage was executed, in place of another printing press, and that the consent of the corporation to the mortgage did not apply to the substituted mortgage." The court in General Term held that a purchaser of property of a corporation at execution sale under judgments against it, who had notice of a prior mortgage on the property, could not take advantage of the alleged want of consent to the mortgage by the corporation, as required under the laws of New York. The court concluded its opinion in these words: "But even if it were conceded that the assent of the corporation should have been obtained to the execution of these mortgages, such assent was in fact obtained. The assent of the corporation, as set forth in writing and filed, was an assent 'that the real and personal property of the Star Printing Company may be mortgaged.' This language was broad enough to warrant the canceling of the mortgage on some of the chattels of the company, with the consent of all parties to the mortgage, and the substitution of another mortgage on other chattels of the company. This assent was not

[1] Brown *v.* Grand Rapids Parlor Furniture Co., (1893) 58 Fed. Rep. 286. As to chattel mortgages by corporations, see Cooper *v.* Corbin, 105 Ill. 224; Hoyle *v.* Plattsburgh & Montreal R. R. Co., 54 N. Y. 315; Nichols *v.* Mase, 94 N. Y. 160; Williamson *v.* New Jersey Southern R. R. Co., 29 N. J. Eq. 311; Bement *v.* Plattsburgh & Montreal R. R. Co., 47 Barb. 104; Kelly *v.* Boylan, 32 N. J. Eq. 581; Stevens *v.* Buffalo & New York City R. R. Co., 31 Barb, 590.

of itself a mortgage, but only a permission to mortgage, and authorized the substituted mortgage in question. It should be borne in mind that the objection [object?] of the legislature in requiring such assent was the protection of stockholders against improvidence, collusion or unwise acts of the trustees, the governing body of the corporation, in incumbering the corporate property. Bank *v.* Averell, 96 N. Y. 473. There is no reason to believe that it was any part of the intention of the legislature to supply purchasers of corporate property with means of defeating the just claims of *bona fide* creditors of a corporation, when the existence of such claims, and of the liens depending thereon, were well known to the purchaser, and the justice and validity of such claims were unimpeached." [1]

§ 513. Deeds of trust and mortgages securing directors — when properly given.— The contention here was that the deed of trust executed by this railroad company upon certain lands belonging to it was void because of its execution to secure debts due to certain of its directors, also large holders of its stock and mortgage bonds. The court held, however, that the inducement of the directors being to protect and give value to their own large interests as creditors and stockholders, but all other creditors and stockholders being equally protected thereby, the advances made in good faith by them, and used for legitimate corporate purposes, constituted a valid debt, enforceable by suit, and the deed of trust thereafter executed by the direction of the stockholders and board of directors to secure it was as valid as if given to any other creditor.[2] It was further held that, treating the directors as trus-

[1] Star Printing Co. *v.* Andrews, (1890) 9 N. Y. Supp. 731, 732.

[2] Gould *v.* Little Rock, M. R. & T. Ry. Co., (1892) 52 Fed. Rep. 680. CALDWELL, Circuit Judge, in support of the rule declared in the text, said: "Where a corporation is legally liable to pay a debt it may undoubtedly give security for its payment. The use of its property to pay or secure a *bona fide* debt is not an unlawful use or diversion of its property, no matter what official relation the creditor sustains to the corporation. The corporation is under the same obligation to pay a *bona fide* debt due to one of its directors and stockholders that it is to pay a debt due to a stranger, and a security given for a debt due to a director and stockholder is as valid as a security given to pay other creditors. The doctrine established by the best-considered cases and by the decisions of the Supreme Court of the United States is that the mere fact that creditors of a corporation are directors and stockholders does not prevent their taking security to themselves as individuals to secure a *bona fide* loan of money previously made to such corporation and

tees, the payment of the debt was an essential prerequisite to the avoidance of the deed of trust given to secure it, whether the debt was a present or precedent one.[1] In a chancery case in New Jersey it appeared that there were a number of mortgages

used by it in conducting its legitimate corporate business. Among the states maintaining this doctrine may be mentioned Vermont, Massachusetts, Connecticut, New York, New Jersey, Pennsylvania, Virginia, Illinois, Minnesota and Iowa. The rule is thus stated in a recent case by the Supreme Court of Iowa: 'We understand that he [a director] may become a creditor of the corporation, may advance it money or sell it property, and obligations of the corporation executed therefor may be enforced by him. In this regard he occupies no different position from that of any other creditor, and if the debt he holds was contracted in good faith and there is an absence of fraud on his part he may take security or payment, though the corporation be insolvent, and he may thereby acquire priority in the payment of his claim.' Garrett *v.* Plow Co., 70 Iowa, 697; s. c., 29 N. W. Rep. 395. The previous cases in that court to the same effect are: Buell *v.* Buckingham, 16 Iowa, 284; Bank *v.* Wasson, 48 Iowa, 336; Hallam *v.* Hotel Co., 56 Iowa, 178; s. c., 9 N. W. Rep. 111. In discussing the question the Supreme Court of Connecticut say: 'These creditors had a perfect right to receive pay in money or goods, and the fact that they were stockholders and directors did not modify or abridge that right so long as there was no actual fraudulent intent. The fact, if it be a fact, that it operated to prefer these creditors, is not sufficient at common law to stamp it as fraudulent, for the common law favored the vigilant and a creditor might rightfully obtain a preference.' Smith *v.* Skeary, 47 Conn. 47. And to the same effect see Duncomb *v.* Railroad Co., 84 N. Y. 190; 88 N. Y. 1; Harts *v.* Brown, 77 Ill. 226; Reichwald *v.* Hotel Co., 106 Ill. 439; Stratton *v.* Allen, 16 N. J. Eq. 229; Wilkinson *v.* Bauerle, 41 N. J. Eq. 635; s. c., 7 Atl. Rep. 514; Bank *v.* Whittle, 78 Va. 737; Ashhurst's Appeal, 60 Penn. St. 314; Whitwell *v.* Warner, 20 Vt. 425; Gordon *v.* Preston, 1 Watts, 386; Sargent *v.* Webster, 13 Met. 497; Kitchen *v.* Railway Co., 69 Mo. 224; Oil Co. *v.* Marbury, 91 U. S. 587. An exhaustive and luminous discussion of this question is found in the opinion of the Supreme Court of Minnesota, delivered by Judge MITCHELL, in the case of Hospes *v.* Car Co., (Minn.) 50 N. W. Rep. 1117. The reasoning of the learned judge who delivered the opinion of the court in that case makes it extremely clear that an insolvent corporation may prefer its creditors, whether they be officers of the corporation or strangers, and that there is no foundation for the doctrine that the insolvency of a corporation has the effect to convert its assets into a trust fund in the technical sense of that term, and its officers into mere trustees charged with the duty of distributing its assets ratably among its creditors. The question has been before the Supreme Court of the United States in several cases. In the case of Hotel Co. *v.* Wade, 97 U. S. 13, the court said: 'His [circuit judge's] finding is that the bonds and mortgages were not void upon the ground that the lenders of the money were also the directors of the company; that the terms of the

[1] Gould *v.* Little Rock, M. R. & T. Ry. Co., (1892) 52 Fed. Rep. 680, 686. See Duncomb *v.* Railroad Co., 84 N. Y. 190; 88 N. Y. 1. When directors

executed by a corporation to the directors of the corporation upon the eve of application for a receiver of the corporation as insolvent. The corporation was limited by its charter in its authority to mortgage to a limited amount. At the time these mortgages were executed it had about exhausted its power to raise money by mortgage under its charter. There was a contention that as a consequence these mortgages were *ultra vires*, and since, not for cash loaned, but as security for previous advancements, or against the indorsements of these directors, they were void as to general creditors and could not be enforced in equity. It was also insisted upon the part of the receiver of the insolvent corporation that the mortgages executed by the corporation to its directors and others were illegal and void as to creditors, because conceived in fraud and for the purpose of cheating, delaying and hindering the creditors. Vice-Chancellor BIRD held that, under the Corporation Act of the state of New Jersey, as revised, the directors of a corporation may execute to themselves mortgages to secure the actual or contingent liability of the corporation to themselves, even though it be done in contemplation of imme-

contract were sanctioned by the stockholders, and that the money loaned was needed to complete the building, and that it was applied to effect the purpose for which it was borrowed. * * * Examined in the light of the circumstances attending the transaction, as the case should be, the court is of the opinion that the finding fails to support the proposition that the bonds and mortgage were invalid because the directors became the holders of the bonds and advanced the money. Transactions of the kind have often occurred, and it has never been held that the arrangement was invalid where it appeared that the stockholders were properly consulted and sanctioned what was done either by their votes or silence.' In the case of Richardson's Exr. *v.* Green, 133 U. S. 30, 43; s. c., 10 Sup. Ct. Rep. 280, the court said: 'Undoubtedly, his relation as a director and officer or as a stockholder of the company does not preclude him from entering into contracts with it, making loans to it and taking its bonds as collateral security; but courts of equity regard such personal transactions of a party in either of the speositions, not perhaps with distrust, but with a large measure of watchful care, and, unless satisfied by proof that the transaction was entered into in good faith, with a view to the benefit of the company as well as of its creditors, and not solely with a view to his own benefit, they will refuse to lend their aid to its enforcement.' "

may execute mortgages to themselves: Whittaker *v.* Amwell Nat. Bank, (N. J. Eq.) 29 Atl. Rep. 203; Brown *v.* Grand Rapids Parlor Furniture Co., 58 Fed. Rep. 286; s. c., 7 C. C. A. 225. Execution of mortgage notwithstanding pending insolvency: Sabin *v.* Columbia River Lumber & Fuel Co., (Or.) 34 Pac. Rep. 692.

diate application for the appointment of a receiver, and the lien secured by such mortgagees would be valid and prior to the liens of general creditors, which was contrary to the statute as it existed prior to the revision.[1] The mortgage of the plant of a corporation which was in course of foreclosure in favor of certain officers and directors of the corporation, to whom it was given as a security or indemnity against loss by the loaning of their credit to the corporation, was claimed before the Supreme Court of Nebraska to be void by reason of the fact that the plaintiffs were directors of the corporation at the time the indebtedness was incurred and when the mortgages were executed. The court held the mortgage to be valid and enforceable.[2] In case a corporation, while

[1] Whittaker *v.* Amwell Nat. Bank, (N. J. Eq. 1894) 29 Atl. Rep. 203; citing in support of the rule for construction of the statute adopted, Bowyer *v.* Camden, 50 N. J. Law, 87; s. c., 11 Atl. Rep. 137; Hoetzel *v.* East Orange, 50 N. J. Law, 354; s. c., 12 Atl. Rep. 911; Haynes *v.* Cape May, 50 N. J. Law, 58; s. c., 13 Atl. Rep. 231; Bank *v.* Bridges, 30 N. J. Law, 112; citing as to the validity of the mortgages to directors, Wilkinson *v.* Bauerle, 41 N. J. Eq. 635; s. c., 7 Atl. Rep. 514; Bergen *v.* Fishing Co., 42 N. J. Eq. 397; s. c., 8 Atl. Rep. 523. See Boehme *v.* Rall, (N. J. Eq.) 26 Atl. Rep. 832.

[2] Gorder *v.* Plattsmouth Canning Co., (1893) 36 Neb. 555. The court said: "It should be observed in this connection that two of the plaintiffs * * * were acting as president and secretary respectively, and as such executed the mortgages in behalf of the company. There is no claim made of fraud against the plaintiffs. In fact their conduct throughout proves that they were actuated by no motives but to promote the success of the company and the interest of the stockholders. It is not disputed that the business of the company was conducted from the beginning with money raised by these and other directors upon their personal obligations. And, from the facts disclosed by the record, the inference is irresistible that said money was advanced, and that the mortgages to the plaintiffs were executed, with the knowledge and approval of the stockholders, including the interveners [who were opposing the foreclosure].' After instancing various things appearing in the record to justify such inference, the court further on said as to the one intervener who positively denied knowledge of the mortgages, "We think, in view of the undisputed facts in the case, he should not now be heard to question this legality. He, in common with other stockholders, must have known from the amount of the company's business, that it was obtaining large sums of money from some source and beyond its power to secure except by mortgaging the canning factory and fixtures. It is also in evidence, and not seriously questioned, that at each annual meeting of the stockholders a statement of the assets and liabilities of the company was exhibited and the books examined. When we take into consideration also the fact that the validity of the mortgages was first called in question by the interveners' answer, * * * it is evident that the claim of the latter that the execution thereof was without their consent is not entitled to serious consideration."

still a going concern, is insolvent, a mortgage on its property, executed to secure directors, who are liable as indorsers for it to a large amount, is valid as to general creditors, and that though the mortgage may be procured by the directors without any actual fraudulent intent.[1] The Supreme Court of Iowa has held that a trust deed made by an insolvent corporation, and conveying nearly all its property, was not void on the ground that it was given to secure only a portion of its creditors.[2]

§ 514. The validity of mortgages as affected by restrictions, constitutional, statutory or in charter, upon indebtedness to be incurred.— The Supreme Court of Pennsylvania having sustained the power of this railroad company, under the charter of 1837 and the subsequent act of the legislature of 1853, then considered an objection to the validity of this mortgage, which was that there was in issuing these bonds and executing this mortgage to secure them, on the part of the railroad company, an increase of indebtedness without compliance with the provisions of the Constitution of 1874, to the following effect: "No corporation shall issue stock or bonds, except for money, labor done, or money or property actually received, and all fictitious increase of stock or indebtedness shall be void. The stock and indebtedness of corporations shall not be increased, except in pursuance of general law, nor without the consent of the persons holding the larger amount in value of the stock first obtained, at a meeting to be held after sixty days' notice, given in pursuance of law," and the acts passed subsequently to carry this constitutional provision into effect, prescribing the mode of proceeding, etc., in such cases of contemplated increase of indebtedness. The court held that the mortgage was not invalid as in conflict with this constitutional provision and statute.[3] It was contended in an

[1] Howe, Brown & Co. *v.* Sanford Fork & Tool Co., (1890) 44 Fed. Rep. 231. The court cited in support of this ruling, Lippincott *v.* Carriage Co., 25 Fed. Rep. 577, 586; White, etc., Mfg. Co. *v.* Pettes Importing Co., 30 Fed. Rep. 864; Adams *v.* Milling Co., 35 Fed. Rep. 433; Beach *v.* Miller, (Ill.) 22 N. E. Rep. 464; Haywood *v.* Lumber Co., 64 Wis. 639; s. c., 26 N. W. Rep. 184; Olney *v.* Land Co., 16 R. I. 597; s. c., 18 Atl. Rep. 181; Rouse *v.* Bank, (Ohio) 22 N. E. Rep. 293; Hope *v.* Salt Co., 25 W. Va. 789; Gillet *v.* Moody, 3 N. Y. 479; Purifier Co. *v.* McGroarty, 136 U. S. 241; s. c., 10 Sup. Ct. Rep. 1017.

[2] Rollins *v.* Shaver Wagon & Carriage Co., (1890) 80 Iowa, 380; s. c., 45 N. W. Rep. 1037; citing as authority Southern White Lead Co. *v.* Haas, 73 Iowa, 404.

[3] Gloninger *v.* Pittsburgh & Connellsville R. R. Co., (1890) 139 Pa. St.

earlier Pennsylvania case that the execution of a mortgage by the corporation, party to the suit, was in violation of the same constitutional provision. In the opinion rendered by McCollum, J., for the Supreme Court, holding the instrument to be a valid one, it was said: "It was given to secure a debt incurred by the company in the improvement of its property, and it was clearly within the power of the corporation to create the debt and to execute the mortgage. It could hold, purchase and transfer such real and personal property as its purposes required, not exceeding the amount limited by its charter or by law, borrow money on bond and mortgage, and secure its indebtedness by them. Act of April 29, 1874, P. L. 73. But it is objected that the debt was not authorized by a previous meeting and consent of stockholders. as directed by § 7, article 21 of the Constitution, and the act of April 18, 1874, P. L. 61. This objection assumes that the debt secured by the mortgage was an increase of indebtedness within

13; s. c., 21 Atl. Rep. 211; 27 W. N. C. 497. As to this contention, the Supreme Court of Pennsylvania said: "We have seen that the right of the company to mortgage its property was complete, absolute, and without any conditions or limitations as to the manner of its exercise. There was nothing, either in its charter or its supplemental acts, or in any general legislation prior to the Constitution of 1874, which imposed any restrictions or formalities upon it, in the exercise of its right to increase its indebtedness or to make mortgages upon its property. Neither the act of 1855 nor the amendment of 1857, which gave power to the legislature to alter, revoke or annul charters of the corporation when they were injurious to the citizens of the Commonwealth, had any specific effect upon this particular chartered right of this company." The court then reviewed several cases in that state, including Ahl *v.* Rhoads, 84 Pa. St. 319, and Lewis *v.* Jeffries, 86 Pa. St. 340, in both of which mortgages executed by banks, without conformity to the requirements of the same constitutional provision and statutes, were upheld by this court. They said: "In view of the provisions of the Constitution, that 'The general assembly shall not remit the forfeiture of any corporation now existing, or alter or amend the same, or pass any general or special law for the benefit of such corporation, except upon the condition that such corporation shall thereafter hold its charter subject to the provisions of this Constitution,' and of the schedule that 'All laws in force in this commonwealth at the time of the adoption of this Constitution, not inconsistent therewith, and all rights, actions, prosecutions and contracts, shall continue as if this Constitution had not been adopted;' and in view of the repeated decisions of this court, that neither the Constitution of 1874, nor the legislation to carry it into effect, had any application to existing charters, it is our plain duty to decide, as we now do, that the [article of the Constitution invoked here] is not applicable to [this railroad company], so as to affect its rights and privileges under its charter."

the intendment of the Constitution. It is consonant to reason and settled by authority that the debts incurred by a corporation in the conduct of its ordinary business, are not affected by the constitutional provision, or by the act of assembly referred to."[1] In an action by certain officers and directors, who had loaned their credit to a corporation, to foreclose the mortgages given for their indemnity against loss upon the plant of the company, it was claimed by interveners, other stockholders, that the mortgages were void for the reason that they were in excess of the amount of indebtedness authorized by the articles of incorporation of the company. The Supreme Court of Nebraska sustained the validity of the mortgages over this objection.[2]

§ 515. A mortgage of corporation property to pay purchase-money debts.—The president, secretary and treasurer of a Pennsylvania manufacturing corporation, as the latter was

[1] Manhattan Hardware Co. *v.* Phalen, (1889) 128 Pa. St. 110.

[2] Gorder *v.* Plattsmouth Canning Co., (1893) 36 Neb. 548. The court said: "It is provided by article 4 that 'The highest amount of indebtedness to which the corporation shall at any time subject itself shall not exceed one-half of the amount of its capital stock issued.' It appears from the bill of exceptions that five thousand dollars of the indebtednsss represented by the mortgages was incurred on the 18th day of August, 1885, on which day the plaintiffs executed their joint note to the [national bank] for the accommodation of the company, the note of like amount, described in the mortgages, being a renewal thereof. At that time the amount of stock issued does not appear, although it is alleged in the answer that the capital stock in February, 1885, was eighteen thousand dollars, nor is the amount of the company's indebtedness apparent from the record. It appears, also, from the minutes of a meeting of stockholders, held January 4, 1886, that 148½ shares of stock were represented thereat, from which it is evident that the stock at that date amounted to at least fourteen thousand eight hundred and fifty dollars. The date when the additional indebtedness of forty-five hundred dollars was incurred does not appear, but the note for said amount is in renewal of an accommodation note executed by plaintiffs for the benefit of the company, long prior to the execution of the mortgages. The presumption is in favor of the validity of the contract in question. It is not, upon its face, necessarily outside the scope of the corporate power of the defendant's company. The recognized rule is that the contracts of a corporation not contrary to the express provisions of its charter, are presumed to be within its powers, and the burden is upon one seeking to invalidate them to prove the facts which render them *ultra vires.* Ohio & M. R. Co. *v.* McCarthy, 96 U. S. 267; Curtis *v.* Gokey, 68 N. Y. 300; Elkins *v.* Camden & Atlantic R. Co., 36 N. J. Eq. 241; Wood Law of Railroads, 526; Boone Corp. 43. This case is clearly within the rule recognized in the authorities cited."

about being pressed for the balance of purchase money for real estate purchased by it for its business, borrowed from a third party the money and executed a mortgage in the name of the corporation to secure it. It appeared in the case that these officers of the company had issued to themselves shares of the stock of the corporation and gave their notes for the money secured by these shares as collateral, but the money was applied to the payment of this purchase-money debt of the corporation. The validity of the mortgage was assailed in a bill in equity of certain shareholders, alleging conspiracy to defraud, and charging that the mortgage was executed to secure a private loan to these officers as individuals and also that the mortgage was executed in violation of the provisions of the Constitution of the state as to increase of indebtedness on the part of the corporation. The validity of the mortgage was upheld by the Supreme Court of the state, they holding that the corporation having executed and delivered the mortgage, the money raised therein being admittedly applied to discharge a purchase-money indebtedness on the mortgaged property, the mortgagee receiving, moreover, certain shares of stock of the company with the note of its officers as additional security for the loan, and, as the mortgage did not increase the indebtedness of the corporation, it was not invalid because in violation of the constitutional provision prohibiting such increase without the consent of the shareholders, and, in the absence of fraud, the mortgagee had a right to all the security the company or its officers were willing to give him.[1]

[1] Powell *v.* Blair, (1890) 133 Pa. St. 550; s. c., 19 Atl. Rep. 559, affirming the decree below. In the opinion which was rendered by SCHUYLER, P. J., in the court below, confirming the master's report, upon the last point made it was said: "In Ahl *v.* Rhoads, 84 Pa. St. 319, it is held that where a bank, without the consent of its shareholders, executes a mortgage upon its property to secure the debt of a creditor, the execution of such a mortgage is not an increase of indebtedness within the meaning of the Constitution, which prohibits any increase of indebtedness by a corporation without the consent of a majority of its stockholders given at a meeting called for that purpose. The ground of that decision is that the mortgage was given as 'security for indebtedness that had already legitimately accrued,' and that, therefore, 'there was nothing in the transaction that could be properly described as the creation or increase of a debt.' We cannot see wherein Ahl *v.* Rhoads differs in principle from the case in hand. True, in the former case the mortgage was given immediately to the creditor, but the effect in both cases was the same, the securing of an existing debt."

§ 516. **Illustration of an equitable mortgage.**—As to who might resist the payment of this fraudulent judgment, it appeared that two railroads, owned by a Tennessee company and a Georgia company, were constructed to form one line and as a common enterprise, the controlling interest in the stock of each being held by the same parties. The Tennessee company agreed with the contractor who built its road to pay him in mortgage bonds at a fixed rate per mile. The bonds actually delivered to and sold by him were, however, issued by the Georgia company, but the Tennessee company gave a mortgage on its road to secure them. The Court of Appeals held that the persons acquiring these bonds had an equitable mortgage on the road of the Tennessee company, such as would entitle them to contest the fraudulent judgment which gave to sub-contractors fictitious liens on the road. As to the right of parties to raise objections to this equitable mortgage, it was held that the sub-contractors could not object to the mortgage on the ground that it was given by the railroad company when insolvent, and was, therefore, void under the Tennessee law. Their claim, if they had any at all against the company, being a lien prior to the mortgage, and, if they had no claim against the company, but only against the principal contractor, then they had no interest in any disposition the company might make of its property. Neither could a general creditor, whose claim came into existence subsequent to the execution of the mortgage, object to it on the ground of an unlawful preference. There was an objection to this mortgage that there was no power in the company to execute it by reason of the provisions of the Tennessee statute which provides that no railroad company shall have power to execute any mortgage or other lien which shall be valid as against judgments for work and labor done or timbers furnished, etc. The Court of Appeals held that this statute applied only when the labor and materials were furnished in such manner that the railroad company would be liable to pay the contractor or materialman for them, and not when they were furnished to a principal contractor in his individual capacity without establishing a lien in the manner prescribed by the later statute relating to railroads contracting liens; and, further, if, in the latter case judgments were fraudulently obtained against the company, the statute would not prevent a court of equity disregarding them.[1]

[1] Central Trust Co. of New York *v.* Bridges, (1893) 57 Fed. Rep. 753.

§ 517. **Mortgage of a consolidated railroad company — estoppel to claim its invalidity on the ground that the consolidation was not legally perfected.**— Certain local railroad companies in the state of South Carolina, which had been aided by counties of that state subscribing to their capital stock, looking to securing the greatest benefits to the separate companies and accomplishing the purposes which led counties through which they passed to aid in the construction of the respective roads under the laws of South Carolina, were consolidated under a general corporate name. This consolidated organization executed a mortgage to a trust company to secure bonds which it issued, the latter being used principally for taking up the divisional bonds issued by the separate companies and for use in part in completion and perfection of the roads of the system. The trustee brought action to foreclose this mortgage in the federal court. The suit was resisted by a cross-bill filed by several of these counties which held stock in the separate roads and afterwards in that of the consolidated mortgage. It was contended that the mortgage was an invalid one. One of the questions raised was as to the consolidation. From the statement of the court, it appeared that the agreement entered into was in compliance with the general statute of South Carolina upon the subject of consolidation of roads, and was executed by each board of directors and submitted to the stockholders of the several companies. The minutes of the action of three of the companies confirming the agreement were in evidence, but the minutes of the other company had been lost. The old stock was surrendered and the new certificates accepted. The new company took full charge and control of all the roads embraced in the agreement, without question or exception, and for years exercised such control, with immense advantage to the different roads from the consolidation. The court held that such facts showed that the agreement was accepted and ratified; also, that it was not an essential prerequisite to such consolidated companies acting as a corporation that the agreement should have upon it the certificates of the several secretaries of each of the railroad companies that it had been accepted. After disposing of this question, it was held further that the organization having assumed to act as a corporation, and issued the bonds secured by the mortgage and put the bonds in circulation, persons holding stock in the corporation, as such, could not

defeat the bonds and mortgage by alleging that the corporation was not duly incorporated.[1] The court held the mortgage valid over the objection that it was not submitted to the corporation for approval, but was the act of its directors.[2]

§ 518. **Illustration of a fraudulent mortgage.**— A Michigan manufacturing corporation having, in carrying on its business, become involved with a large floating indebtedness, certain new parties, with a view to paying this floating indebtedness, were brought into it. There were subsequent readjustments of the stock of the corporation, which resulted finally in one of those

[1] Phinizy *v.* Augusta & K. R. Co.; Central Trust Co. of New York *v.* Port Royal & Western Carolina Ry. Co., (1894) 62 Fed. Rep. 678. The court said in one place: "It must be kept in mind that the consolidation of railroads does not create a new corporation, with powers of its own, distinct from, greater or less than, those enjoyed by the consolidating companies separately. It is a method provided by law for the formation of a copartnership between railroad corporations, by which, if the expression may be used, they pool their franchises and property, and are enabled to act in complete harmony under one head, as a unit. This unit possesses the powers of its component parts — no more and no less. Pub. Laws, § 1538 (Gen. St. S. C. § 1427). And the act authorizing it provides a method of advertising the state that this copartnership has been formed. No further grant of a franchise is necessary, nor is any given. Indeed, it is an accomplished fact, requiring no further act or deed on the part of the state, or any one else. Gen. St. § 1428 (Pub. Laws, § 1539)." See, also, Wallace *v.* Loomis, 97 U. S. 146.

[2] Phinizy *v.* Augusta & K. R. Co.; Central Trust Co. of New York *v.* Port Royal & Western Carolina Ry. Co., (1894) 62 Fed. Rep. 678. It was said by the court: "Under the law of South Carolina (Gen. St. S. C. §§ 1427, 1428; Pub. Laws S. C. §§ 1538, 1539) it is provided that, upon the consummation of the act of consolidation, the rights, privileges and franchises of each of the corporations, parties to the same, shall be taken and deemed to be vested in and transferred to such new corporation, without any further act and deed. Each of these corporations, at the date of the consolidation, had outstanding bonds secured by mortgage under proper authority. The main purpose of the new mortgage was to take up them and substitute the bonds of the new company. The bonds and mortgage substituted were authorized and sustained by the same powers. 'The directors alone, without the vote of the stockholders, may authorize a mortgage to be made; and even though there is a question as to their authority, the validity of the mortgage, as against the corporation, is established by its affirmance of it by the issue of bonds under it.' Wood R. R. 1951, § 461, quoting McCurdy's Appeal, 65 Pa. St. 290; Hodder *v.* Railroad Co., 7 Fed. Rep. 793. 'If the act authorizing the mortgage requires a concurrence of the majority of stockholders, it is held that this is a requirement in which the public have no interest.' Thomas *v.* Railroad Co., 104 Ill. 462."

who had assumed this floating indebtedness having one share of the stock issued to his brother, and there was a new election of officers. The two brothers, one as president, and the other as secretary and treasurer, and the third party as vice-president, were elected. A meeting of the directors was then called and a resolution adopted, the two brothers voting for it, the third party against, which authorized the execution of a chattel mortgage upon the whole plant and stock to secure a large note then held by transfer to him by their father. Under a bill for foreclosure of this mortgage a receiver was appointed and a decree for sale, and the property was sold and purchased by the father and a bank holding the other note, these notes representing the original floating indebtedness which the defendant in this action assumed. The declaration alleged that the introduction of the brother of this defendant into the corporation, the readjustment of the shares of stock, the change made in the officers of the corporation, the transfer of the notes, the resolution directing the execution of the chattel mortgage, and the sale of the property, were acts done in pursuance of a fraudulent scheme to relieve the former president of the corporation from his obligations, to appropriate the assets, goods and plant, and deprive the plaintiff, the only other shareholder, of his interest in the corporation, and that the defendants unlawfully conspired together to accomplish the desired purpose. The Supreme Court of Michigan held that the declaration set forth a cause of action. They said: "The right of the directors of a corporation to execute a mortgage to secure its indebtedness does not include the right of a member of that corporation, who is under obligations to carry the corporation paper, to introduce a dummy into the board of directors, and, confederating with him, direct the execution of a mortgage to another confederate, to whom the paper has been assigned for the purpose of avoiding these obligations, wrecking the corporation and appropriating its assets; nor does the right of a creditor to foreclose include the right of such confederate fraudulently to obtain the security for the purpose named and to foreclose it in furtherance of that purpose." [1]

§ 519. **What corporation mortgages cover, and what they do not cover.**— It is settled that the after-acquired property

[1] Hanley *v.* Balch, (1892) 94 Mich. 315, 319.

clause in a mortgage of railroad property is valid, and that thereby the mortgage covers not only property then owned by the railroad company, but becomes a lien upon all property subsequently acquired by it which comes within the description in the mortgage.[1] And this is true, not only as to property to which it acquires the legal title, but also as to that to which it acquires only a full equitable title.[2] The doctrine that the "after-acquired property" clause in a railroad mortgage covers not only legal acquisitions, but also all equitable rights and interests subsequently acquired either by or for the railroad company, has been reaffirmed by the Supreme Court of the United States.[3] The language of a railroad mortgage covering, among other things, all the corporate rights, privileges, franchises and immunities, and all other things in action, contracts, claims and demands of the said party of the first part, whether now owned or hereafter acquired in connection or relating to said railroad, has been held sufficient to include a subsequently acquired lease of a belt railway whereby the company acquired access to a city at one of its termini.[4] A lien will be created upon the terminal facilities of a railroad company where such company is incorporated to construct a railroad between two cities named as its termini, by a mortgage, expressed to be upon its line of railroad constructed, or to be constructed, between the named termini, together with all the stations, depot grounds, engine houses, machine shops, buildings, erections in any way now or hereafter appertaining under

[1] Central Trust Co. *v.* Kneeland, (1891) 138 U. S. 414. See Pennock *v.* Coe, 23 How. 117; Dunham *v.* Cincinnati, P., etc., Ry., 1 Wall. 254; Galveston Railroad *v.* Cowdrey, 11 Wall. 459; Thompson *v.* Valley Railroad Company, 132 U. S. 68; Omaha & St. Louis Ry. Co. *v.* Wabash, St. Louis & Pac. Ry. Co., (1891) 108 Mo. 298; McTighe *v.* Macon Construction Co., (Ga.) 21 S. E. Rep. 701.

[2] Toledo, etc., Railroad Co. *v.* Hamilton, 134 U. S. 296. The court cited in support of this position Jones on Mortgages, § 138; Massey *v.* Papin, 24 How. 362; Farmers' Loan & Trust Co. *v.* Fisher, 17 Wis. 114; Lincoln Building Assn. *v.* Hass, 10 Neb. 581; Laughlin *v.* Braley, 25 Kans. 147.

[3] Wade *v.* Chicago, Springfield & St. Louis R. R. Co., (1893) 149 U. S. 327; s. c., 13 Sup. Ct. Rep. 892; citing Dunham *v.* Cincinnati, P., etc., Ry. Co., 1 Wall. 254; Galveston Railroad *v.* Cowdrey, 11 Wall. 459; Porter *v.* Bessemer Steel Co., 122 U. S. 267; Toledo, etc., Railroad *v.* Hamilton, 134 U. S. 296; Central Trust Co. *v.* Kneeland, 138 U. S. 414. As to the priority of a railroad mortgage covering after-acquired property under the Iowa statutes, on rolling stock delivered to the railroad company, before its use, on the depot grounds, see Manhattan Trust Co. *v.* Sioux City & N. Ry. Co., 68 Fed. Rep. 72.

[4] Columbia Finance & Trust Co. *v.* Kentucky Union Ry. Co., (1894) 60

the described line of railroad, and will not be limited to so much of the road as is found between the city limits of those places.[1] A railroad mortgage on an entire line of railroad between named points, "as said railroad now is or may be hereafter constructed, maintained, operated or acquired, together with all the privileges, rights, franchises, real estate, right of way, depots, depot grounds, side tracks, water tanks, engines, cars and other appurtenances thereto belonging," has been held by the Supreme Court of Missouri to cover land subsequently purchased by the company near a depot on the line of its road, and a hotel erected thereon for the purpose of an eating house and to accommodate the

Fed. Rep. 794; citing Trust Co. *v.* Kneeland, 138 U. S. 416; s. c., 11 Sup. Ct. Rep. 357; Railroad Co. *v.* Hamilton, 134 U. S. 297; s. c., 10 Sup. Ct. Rep. 546; Branch *v.* Jesup, 106 U. S. 468; s. c., 1 Sup. Ct. Rep. 495. As to what such mortgages cover, see Cooper *v.* Corbin, 105 Ill. 224; First Nat. Bank of Salem *v.* Anderson, 75 Va. 250; Nichols *v.* Mase, 94 N. Y. 160; McAllister *v.* Plant, 54 Miss. 106; Morgan & Raynor *v.* Donovan, 58 Ala. 241; Kelly *v.* Trustees, 58 Ala. 489; Butler *v.* Rahm, 46 Md. 541; Pullan *v.* Cin. & Chic. Air Line R. R. Co., 5 Biss. 237; Calhoun *v.* Memphis & Paducah R. R. Co., 2 Flip. 442; Seymour *v.* Canandaigua & Niagara Falls R. R. Co., 25 Barb. 284; Willink *v.* Morris Canal & Bkg. Co., 4 N. J. Eq. 377; Eldridge *v.* Smith, 34 Vt. 484; Elwell *v.* Grand St. & Newtown R. R. Co., 67 Barb. 83; Farmers' Loan & Trust Co. *v.* Commercial Bank of Racine, 15 Wis. 426; Farmers' Loan & Trust Co. *v.* Commercial Bank, 11 Wis. 207; Farmers' Loan & Trust Co. *v.* Fisher, 17 Wis. 114; Fisk *v.* Potter, 2 Abb. Ct. App. Dec. 138; Buck *v.* Memphis & Little Rock R. R. Co., 4 Cent. L. J. 430; Galena & Chic. U. R. R. Co. *v.* Menzies, 26 Ill. 121; Bardstown & Louisville R. R. Co., Metcalfe, 4 Metc. (Ky.) 199; Hunt *v.* Bullock, 23 Ill. 320; Ludlow *v.* Hurd, 1 Disney, 552; Mobile & Cedar Point R. R. Co. *v.* Talman, 15 Ala. 472; Morrill *v.* Noyes, 56 Me. 458; Parkhurst *v.* Northern Central R. R. Co., 19 Md. 472; Phil., Wilm. & Balt. R. R. Co. *v.* Woelpper, 64 Pa. St. 366; Pierce *v.* Emery, 32 N. H. 484; Phillips *v.* Winslow, 18 B. Mon. 431; Pierce *v.* Milwaukee & St. Paul R. R. Co., 24 Wis. 551; Robinson *v.* Atl. & Gt. West. Ry. Co., 66 Pa. St. 160; Shamokin Valley R. R. Co. *v.* Livermore, 47 Pa. St. 465; Walsh *v.* Barton, 24 Ohio St. 28; Youngman *v.* Elmira & Williamsport R. R. Co., 65 Pa. St. 278; Parish *v.* Wheeler, 22 N. Y. 494; Morgan County *v.* Thomas, 76 Ill. 120; Raymond *v.* Clark, 46 Conn. 129; Buck *v.* Seymour, 46 Conn. 156; Palmer *v.* Forbes, 23 Ill. 301; Farmers' Loan & Trust Co. *v.* Hendrickson, 25 Barb. 484; Beardsley *v.* Ontario Bank, 31 Barb. 619; Taylor *v.* Burlington, Cedar Rapids & Minn. Ry. Co., 4 Dill. 570; Addison *v.* Lewis, 75 Va. 701; Dean *v.* Biggs, 25 Hun, 122; Titus *v.* Mabee, 25 Ill. 257; Resor *v.* Ohio & Miss. R. R. Co., 17 Ohio St. 139. For an illustration of what was, and what was not, covered by the "after-acquired" property clause in a corporation mortgage, see Boston Safe Deposit & Trust Co. *v.* Bankers & Merchants' Telegraph Co., (1888) 36 Fed. Rep. 288.

[1] Central Trust Co. *v.* Kneeland, (1891) 138 U. S. 414. Mr. Justice

employees of the company, passengers and other persons.[1] It has been held by the United States Circuit Court of Appeals for the fifth circuit that a mortgage by a railroad company of all and any interest the company might have to the land granted to it by the state of Florida to which it had been donated under the act of congress as to the swamp and overflowed land, passed whatever title the company had, as it had a full equitable title, though it did not have a legal title to the land, by reason of the absence of a patent in the original grant to the state.[2] The congress of the United States by act granted the right of way to the state of Missouri through certain public lands between designated points, and also granted to the state every alternate section of land, properly designated by metes and bounds, for the purpose of aiding in making railroads and branches, and at the same time authorized the legislature to dispose of the lands for the purpose named, and for none other. The state by act afterwards granted some of these lands to a railroad company for the purposes above stated and subject to the terms of the acts of congress, and at the same time authorized the company to issue bonds and secure the same by mortgage on those lands in order to raise funds to construct the railroad. By subsequent legislation the state was authorized to issue aid bonds to this company, none of the bonds to be delivered to the company until it had signified its accept-

BREWER, speaking for the court, said: "The stations, depot grounds, etc., in the terminal cities appertain to the railroad as fully as similar structures in places intermediate those termini. In the absence of restrictive words such is the natural import, and, therefore, must be adjudged the intent and scope of a mortgage containing that description. The first mortgage contains not only the general terms referred to, but after them, and as if it were to avoid any possible doubt, adds: 'And all its depot grounds, yards, sidings, turnouts, sheds, machine shops, leasehold rights, and other terminal facilities now or hereafter owned by the said party of the first part.' It would be difficult to make language more full, accurate and descriptive." See Willink *v.* Morris Canal & Bkg. Co., 4 N. J. Eq. 377; Morris & Essex Railroad *v.* Central Railroad Co., 31 N. J. L. 205; Mohawk Bridge Co. *v.* Utica & Schenectady Railroad, 6 Paige, 554; Commonwealth *v.* Erie & Northeast Railroad, 27 Pa. St. 339.

[1] Omaha & St. Louis Ry. Co. *v.* Wabash, St. Louis & Pac. Ry. Co., (1891) 108 Mo. 298. See U. S. Trust Co. of New York *v.* Wabash, St. L. & Pac. Ry. Co., 32 Fed. Rep. 480, where the court ordered the money arising from insurance on the building paid over to the receiver, who represented the first mortgage creditors. The court distinguished Humphreys *v.* McKissock, Receiver, 140 U. S. 304.

[2] Augusta, Tallahassee & Gulf R. Co. *v.* Kittel. (1892) 52 Fed. Rep. 63.

ance by filing a receipt therefor with the secretary of state, and that when recorded in the office of the secretary of state each certificate should be a mortgage on the road. The company accepted these bonds and filed the certificates required, and afterwards the state's statutory mortgage lien upon the railroad and its property was enforced by sale. After the donation of these public lands to the company by the state the company made a deed of trust to certain trustees of these lands to secure an issue of bonds, with power in the trustees to sell these lands and take up the bonds, etc. This case was an ejectment case growing out of the sales of these lands for the purposes above stated, and the question was before the court as to what the statutory mortgage of the state covered. It was held by the Supreme Court of Missouri that the lien of the certificates of the company accepting the aid, which by the provisions of the aid act were to be a mortgage "of the road and every part and section thereof and its appurtenances," did not include the railroad lands granted to the company by the state, since they were not appurtenant to the road. Nor did the lien created by the terms of a subsequent act of the legislature authorizing an additional loan of state bonds to this company where the provision was that the bonds so issued "should constitute a first lien or mortgage upon the road and property of the several railroad companies receiving them" extend the state's lien over such railroad lands granted to the state and by the state to the company.[1] A mortgage of all of the property of a corporation formed to supply heat to the public, covers all the franchises essential to the operation of its property.[2] The United States Circuit Court of Appeals for the

[1] Wilson *v.* Beckwith, (1893) 117 Mo. 61; s. c., 22 S. W. Rep. 639. The court discuss and distinguish Whitehead *v.* Vineyard, 50 Mo. 30; Wilson *v.* Boyce, 92 U. S. 323; Chouteau *v.* Allen, 70 Mo. 290, 327; Railroad *v.* McGee, 115 U. S. 469. In McIlhenny *v.* Binz, (Tex.) 13 S. W. Rep. 655, the directors of a railroad company adopted a resolution authorizing a mortgage of its property to render effectual what was attempted to be done in a former mortgage, the validity of the latter being in doubt. As directed by the resolution, the second mortgage was executed. In this latter there was no reference made to the former, and neither the resolution of the directors nor the second mortgage gave expression to any intention that the same property named in the first mortgage should be covered by the second. The Supreme Court of the state of Texas held that in such case the description of the property in the second mortgage could not be decided by that in the first.

[2] Pumphrey *v.* Threadgill, (Tex. Civ. App.) 28 S. W. Rep. 450.

seventh circuit, upon an appeal from an order in a creditor's bill against a water company and the purchasers of its property at foreclosure sale and others, appointing a receiver and ordering the purchasers to surrender the property to the receiver and restraining these purchasers from interfering with the possession of the receiver, sustained the validity of the mortgage and set aside the order of injunction. It was held that the mortgage executed by the water company covered all franchises owned by the company and enumerated in the ordinance of the city granting the same to the company whether the franchises were in fact granted by the city or by the state.[1] After mortgaging its

[1] Andrews *v.* National Foundry & Pipe Works, (1894) 61 Fed. Rep. 782. It was said by the court upon the construction of the mortgage: "The appellants, it is not disputed, advanced large sums of money to the water company in the belief that they were receiving a valid security, and, while they are presumed to have known the law, it is not to be presumed, if there is reasonable escape from it, that either party to the transaction intended a vain thing. '*Interpretatio facienda est ut res magis valeat quam pereat*,' and other familiar maxims, lend support to the requirement that a contract or deed shall be so construed as to have effect rather than so as to be made void. By the literal terms of the mortgage and of the decree of foreclosure, upon which the title of the appellants depends, there was a conveyance or assignment of 'all the rights, privileges, immunities, franchises and powers, of whatever name or nature, which were granted in and by that certain ordinance,' etc., and if, upon a proper interpretation of the statutes touching this question, no mortgageable right, privilege or franchise was granted in or by the ordinance, as distinguished from a direct grant by the corporation, then by a strict construction the mortgage was, as it was held to be, ineffectual and meaningless. But not by the words alone should a writing be interpreted. 'The rule is to regard the intention rather than the words;' and here the evident intention, deducible from the whole instrument, was to mortgage the rights and franchises which the ordinance granted in terms, or which it purported to convey. The resolution whereby the water company declared its acceptance of the ordinance, and 'of the franchise thereby granted,' shows that both parties entertained an equally broad and generous view of the powers of the common council of the city in the premises, and, when the deed of trust came to be drawn, it was only natural that for certainty of description reference should be made to the ordinance by which the rights of the company were defined, and, as the parties supposed, were granted. And even if this supposition was mistaken, must it be held that the entire purpose of the parties failed, and that, notwithstanding the covenant of the water company that it was 'the owner and holder,' and had 'good right and lawful authority' to make transfer and sale 'of said rights, privileges, immunities, franchises and powers' 'in the manner aforesaid,' yet the instrument is a total nullity? Indeed, why should it not be held that by that covenant the water company is estopped to deny that its franchises were granted by the ordinance? Or must it

property a corporation organized for lighting purposes placed dynamos and exciters in the building used by it for the manufacture of electricity, as part of its electric plant, with the intention that they should remain there till worn out or superseded by more suitable machines. The New York Supreme Court has held that they became part of the realty and were subject to the mortgage as against judgment creditors of the corporation notwithstanding they could be removed without impairing the construction of the building.[1] In a case where several railroad companies combined to construct an elevator connected with their respective railroads, each company agreeing to pay its portion of the cost of construction, and to receive a corresponding amount in the shares of stock in a corporation organized for its construction, and to hold title to the same, the Supreme Court of the United States has held that a railroad company joining in such an arrangement, the elevator to be built upon land not belonging to the company, and situated at some distance from its road, did not acquire an interest in the elevator, which would pass as an appurtenance under a mortgage of its railroad as constructed or to be constructed, and the appurtenances thereto belonging.[2]

be said that the covenant covers only the rights and franchises which were granted by the ordinance, and, like the granting clause, is itself void because the franchise came to the company in that way? It would seem more reasonable, the ordinance having been made a part of the deed by reference as if copied into it, to treat the covenant as covering the rights and privileges named in the ordinance, whether derived from one source or another. To say the least, upon the whole instrument, it is only reasonable and in accord with the canons of construction to read the expression 'which were granted,' etc., as if it were 'which in terms were granted unto the said Oconto Water Company in and by that certain ordinance,' etc. The added words are fairly implied, and the addition, without doing violence to any part of the writing, gives effect alike to the words of grant and covenant and accomplishes the evident purpose for which the deed was executed."

[1] New York Security & Trust Co. *v.* Saratoga Gas & Electric Light Co., 88 Hun, 569; s. c., 34 N. Y. Supp. 890. As to fixtures falling within the terms of a mortgage, see Wade *v.* Donau Brewing Co., (Wash.) 38 Pac. Rep. 1009. As to what is covered by a mortgage, see Wood *v.* Whelen, 93 Ill. 153; Despatch Line of Packets *v.* Bellamy Mfg. Co., 12 N. H. 205; Hicks *v.* Cheyenne Land & Live Stock Co., (Wyo.) 35 Pac. Rep. 475. As to "after-acquired" property, see Wood *v.* Holly Mfg. Co., (Ala.) 13 So. Rep. 948.

[2] Humphreys *v.* McKissock, (1891) 140 U. S. 304; s. c., 11 Sup. Ct. Rep. 779; Wabash, St. Louis & Pacific Ry. Co. *v.* McKissock, Ibid. The court below had passed a decree confirming the report of the commissioners, holding that the mortgaging company possessed such an interest. Upon the

§ 520. Trustees of such mortgages — their duty, rights and powers.— Under the general statutes of Minnesota a railroad company may, in a mortgage executed by it, pledge the income of the property, and, to make such pledge effectual, may

point directly involved Mr. Justice FIELD, speaking for the court, said: "Had the elevator been constructed upon property covered by the mortgage it might have been contended that it fell to the extent of the one-sixth interest under the mortgage, as one of the depots of the company. The term 'depot' in the mortgage is not necessarily limited to a place provided for the convenience of passengers while waiting for the arrival or departure of trains. It applies also to buildings used for the receipt and storage of freight, which, when received, is to be safely kept until forwarded by the cars of the company or delivered to the owner or consignee. Such a building, whether existing at the time of the mortgage or constructed afterwards upon the property of the company covered by it, may pass under the mortgage as one of its depots, but will not pass as an appurtenance to the property previously existing. A thing is appurtenant to something else only when it stands in the relation of an incident to the principal and is necessarily connected with the use and enjoyment of the latter. Harris *v.* Elliott, 10 Pet. 25, 54; Jackson *v.* Hathaway, 15 Johns. 447, 455; Linthicum *v.* Ray, 9 Wall. 241. Of two parcels of land one can never be appurtenant to the other, for though the possession of the one may add greatly to the benefit derived from the other, it is not an incident of the other or essential to the possession of its title or use; one can be enjoyed independently of the other. As said by the Court of Appeals of New York in Woodhull *v.* Rosenthal, 61 N. Y. 382, 390: 'A thing 'appurtenant' is defined to be a thing used with and related to or dependent upon another thing *more worthy*, and agreeing in its nature and quality with the thing whereunto it is appendant or 'appurtenant.' It results from this definition that land can never be appurtenant to other land or pass with it as belonging to it. * * * All that can be reasonably claimed is that the word 'appurtenances' will carry with it *easements* and *servitudes* used and enjoyed with the lands for whose benefit they were created. Even an easement will not pass unless it is necessary to the enjoyment of the thing granted.' Under the term 'appurtenances,' as used in the mortgage in question, only such property passes as is indispensable to the use and enjoyment of the franchises of the company. It does not include property acquired simply because it may prove useful to the company and facilitate the discharge of its business. A distinction is made in such cases between what is indispensable to the operation of a railway and what would be only convenient. Bank *v.* Tennessee, 104 U. S. 493, 496. The elevator in question was at all times under an independent management, and was used in the same manner as any other warehouse not on the premises of the railway company to which it sent cars for freight." In New Orleans & Pac. Ry. Co. *v.* Union Trust Co., (1890) 41 Fed. Rep. 717, the railroad company mortgaged the whole of its line in the state of Louisiana; "also all real and personal estate within the state owned by the company at the date of this mortgage, or which may be acquired by it thereafter, appurtenant or necessary for the

stipulate in the mortgage that upon default the trustee named in the mortgage may take possession, operate the railroad and receive its earnings. Under such a stipulation the trustee, upon default, may, without bringing an action to foreclose, take possession, and, if he be prevented, may have an action to be put in possession.[1]

operation of said line." The special authority given in its charter to the company to mortgage did not authorize it to mortgage an after-acquired land grant. And the Code of Louisiana provided that "future property can never be the subject of conventional mortgage." The federal court for the eastern district of Louisiana held that the mortgage did not affect land thereafter granted to the company to aid in the construction of the road. In New Chester Water Co. *v.* Holly Manufacturing Co., (1892) 53 Fed. Rep. 19, affirming 48 Fed. Rep. 879 (a bill to establish and enforce a lien on pumping engines for the purchase price), where the water company, on a sale of pumping engines for its water works, expressly agreed that the seller, the manufacturing company, should have a lien thereon with full right of possession until the price was paid, the United States Circuit Court of Appeals for the third circuit held that this showed an intent that the pumping engines should not become a part of the realty, and under the Pennsylvania decisions this intent was controlling and the lien was not waived in favor of the mortgage bondholders or other creditors by attaching the engines to the foundation in the usual manner. As to the general rule of law uncontrolled by local statutes governing conditional sales, the court referred to Harkness *v.* Russell, 118 U. S. 663; s. c., 7 Sup. Ct. Rep. 51, as containing an elaborate discussion of the whole subject. They said further: "The present case does not fall within the class of cases * * * in which it has been held that the rails and bridges of a railroad of necessity become a permanent part of the whole structure, and, therefore, cannot be made the subjects of special liens, but is more analogous to the class in which the rolling stock of a railroad company has been held to be the subject of a conditional sale, and on which a lien may be reserved by the vendor. And this appears to be reasonable. Locomotive engines and cars are as essential to the operation of the railroad as pumping engines are to waterworks, but it has been held that the former may be treated as personal property, and as such may be liable to a lien in favor of the seller, which will not be lost in consequence of a prior mortgage which by its terms was made to cover after-acquired property. U. S. *v.* New Orleans & O. R. Co., 12 Wall. 362." In Metropolitan Trust Co. *v.* New York, L. E. & W. R. R. Co., 45 Hun, 84, where there was an agreement by a railroad company with another, as to promoting the business of the former on the part of the latter, in consideration of the latter's giving the former the control of a majority of its stock, and the former road agreed to make good any deficiencies in the net earnings of the latter to meet the interest on its bonds secured by a mortgage of its property by the latter in usual form, the undertaking on the part of the former to make up this deficiency in earnings was held neither to be embraced in nor covered by the mortgage.

[1] Seibert *v.* Minneapolis & St. Louis Ry. Co., (1893) 52 Minn. 246; s. c., 53 N. W. Rep. 1151.

Trustees, under their power in a railroad mortgage, under certain circumstances, as for default in payment of interest for a limited period, to declare all the bonds secured by the mortgages to be past due, must exercise this power with the utmost good faith, and only when approved by their honest, disinterested judgment, as the best thing for the interest of the bondholders.[1] The trustees in a trust deed of a railroad company having, in a suit to be placed in possession of the property, obtained a decree that they are entitled to possession, under the provisions of the trust deed, will be entitled, there being no debts for current expenses, to receive all profits of the road earned from the commencement of their suit.[2] The trustees in a railroad mortgage, having entered into possession of the property by reason of non-payment of the interest on the bonds, according to the terms of the mortgage, where the principal of the bonds has not matured, on the interest being paid, may be compelled to surrender the possession of the property if the mortgage deed in no way requires a course to the contrary.[3] Trustees under a trust deed with covenants of warranty from a railroad company may pay a prior incumbrance to prevent a forced sale of the property embraced in their deed; and when paying such they are subrogated to the rights of the holder of that prior incumbrance.[4] There was a provision in a trust deed executed by a land grant railroad company to secure its bonds that the proceeds arising from the sales of the lands should be applied by the trustees: *First*, to the payment of the interest coupons attached to the bonds, should the earnings of the road be insufficient for their payment; *second*, to the purchase of outstanding bonds at their market value, not exceeding ten per cent premium; *third*, to the payment of bonds coming due. There was also a provision for the investment of the proceeds of the sales not thus used. The holders of certain interest coupons, there being no funds at one time to pay them, accepted scrip of the company, payable in ten years, with the right on the part of the company to take the scrip up at any time. They surrendered their coupons to the trustees, to hold as collateral. The United States Supreme Court held that it was the duty of the trustees at a subsequent time, when

[1] Bound *v.* South Carolina Ry. Co., (1892) 50 Fed. Rep. 853.

[2] Dow *v.* Memphis & Little Rock R. R. Co., 8 Sup. Ct. Rep. 673.

[3] Union Trust Co. *v.* Missouri, Kansas, etc., Ry. Co., 26 Fed. Rep. 485.

[4] Memphis & Little Rock R. R. Co. *v.* Dow, 120 U. S. 287.

the earnings of the road proved sufficient to pay the current coupons, and the business of the company promised that this would continue, and the outstanding bonds of the company could not be bought up on the terms allowed in the trust deed, and investments could not be made except at a lower rate of interest than the scrip held by these former holders of coupons bore, to apply the funds in their hands to the payment of the coupons which were represented by the scrip.[1] A mortgage executed by a railroad company, to secure its bonds, recited that it was deemed expedient to fund certain coupons of prior bonds by the issue of scrip convertible into bonds, and that the bonds which this mortgage was executed to secure had been issued for that purpose. The validity of this mortgage being in doubt, the bonds were destroyed and never issued. Another issue of bonds was made, secured by another mortgage, after which the first mortgage was released by the trustees named therein. In a case before it the Supreme Court of Pennsylvania held that the holders of the coupons referred to in the first mortgage acquired no vested interest in the mortgage which had been released, and that they were in no position to object to the release.[2] The trust companies, acting as trustees in certain railroad mortgages executed by Texas railroad companies, representing the bondholders whose bonds were secured by these several mortgages, brought actions in the United States Circuit Court for the western district of Texas against the railroad companies involved and against the state railroad commissioners and the attorney-general of the state, alleging that the full interest on the bonds was not being paid or earned; that in most cases the earnings were even insufficient to pay operating expenses; that the railroad companies were willing and anxious to meet all their obligations to complainants, but were prevented from exercising their judgment and discretion in making remunerative rates of transportation by the defendant railroad commissioners, under pain of the severe penalties prescribed by the act providing for this board of railroad commissioners. The claim of the bill was that the act was unconstitutional, and prayed for an injunction restraining these commissioners from interfering with the railroad companies in the matters complained of. Their right to maintain the action was questioned before the court.

[1] Little Rock & Ft. Smith Ry. Co. *v.* Huntington, 7 Sup. Ct. Rep. 517.

[2] Commonwealth *v.* Wilmington & N. R. R. Co., (Pa.) 17 Atl. Rep. 5.

The court held, however, that these trustees for bondholders showed a sufficient interest in the roads to entitle them to maintain the suits.[1]

[1] Mercantile Trust Co. *v.* Texas & Pac. Ry. Co., (1892) 51 Fed. Rep. 529. McCormick, Circuit Judge, said: "The complainants here show equitable interest in the fair earnings of the roads; they show actual ownership and possession of the mortgage securities of the roads, both of which they allege are being irreparably injured and threatened with destruction by the defendants; they show that the railways are willing and want to meet all their obligations as mortgagors in possession, but that said railways are coerced by the defendants, armed with the Railroad Commission Act, and the directors cannot exercise their judgment and discharge their duty as they should and would but for said coercion. It may be that the railway companies could, under section 6 of the Railroad Commission Laws, or without the authority of that section, have brought these suits and obtained all the relief to which the complainants are entitled against the other defendants, or it may be that they could not. If they could not, that would be only one additional reason why the complainants should sue; and, if the railways could have so sued, that would be no reason for denying the complainants any right, even if, as seems to be hinted rather than charged, the railways could only have resorted to the state courts; and that there was a previous understanding between the complainants and the railways that the relief complainants desired and believed themselves entitled to receive, would be more likely to be speedily and adequately extended in the national courts. It was to meet such cases that the national courts were established. In them parties 'may hope to escape the local influences which sometimes disturb the even flow of justice.' Davis *v.* Gray, 16 Wall. 221. What has already been said expresses sufficiently my view as to the suggestion, and the authority in its support, that the injury inflicted and threatened, if any, was done and directed to the mortgagor in possession, and is too remote to give the complainants the right to sue. It may be conceded that there is no express decision of the Supreme Court or of other courts of authority on this question, but as to this point the case of Peik *v.* Railway Co., in 94 U. S. 164, is substantially the same as these cases. That case was strongly controverted. Lawyers of the highest national reputation argued it elaborately and at great length in the Supreme Court. The same question was involved in the case of Stone *v.* Trust Co., 116 U. S. 307; s. c., 6 Sup. Ct. Rep. 334, 388, 1191; and while the failure to raise or notice this question in the progress and decision of those cases prevents their being relied on as authority on this point, the fact that it was not raised or noticed is persuasive in the direction of the inclination of my judgment in this case that complainants show a right to one. The case of Murdock *v.* Woodson, 2 Dill. 188, persuades to the same conclusion."

CHAPTER XXVII.

INSOLVENCY OF PRIVATE CORPORATIONS.

§ 521. How far the assets of an insolvent corporation are a trust fund for its creditors.

522. The power of directors of a corporation to execute an assignment of the corporation's property for the benefit of creditors.

523. Preferences of creditors by insolvent corporations.

524. Attachment of property of insolvent corporation — the rights of a creditor to attach — lien of its attachment, etc.

525. Receivers — rules as to appointment.

526. Removal of receivers and assignees.

§ 527. The rights of receivers and assignees as to property of insolvent corporation.

528. Other rights of receivers and assignees of insolvent corporations.

529. Insolvent beneficial association — rules.

530. Liability of stockholders on unpaid subscriptions — the court's right to enforce and how enforced.

531. Creditors' bills — equitable jurisdiction.

532. Claims against insolvent corporation — rules as to allowance, etc.

533. Rules in cases of insolvent banks.

§ 521. How far the assets of an insolvent corporation are a trust fund for its creditors.— The Court of Appeals of West Virginia held that an assignee of an unsound savings bank was entitled to recover from a director of the bank money which he had withdrawn as his deposit in the bank, not in cash, but in bills and notes discounted by the bank, which property of the bank had been turned over to him by the cashier. JOHNSON, President, for the Court of Appeals of West Virginia, then applied the principles evolved from a review of cases to the case before the court, in these words: "It seems to me that the doctrine that the directors of a corporation do not sustain a fiduciary relation to the creditors, is based on no better reason than that a natural person or the member of a partnership do not sustain a confidential relation to their creditors. Is this reason a sound one? Is there no difference between the natural person and the *artificial person* called a corporation? A person goes into mercantile business. He is worth, it may be, one hundred thousand dollars. His creditors trust him more on the faith of his property than his

business management. They know that his liability is unlimited; that all he has is held for his debts. Not so with a corporation. In this state, as well as others, no stockholder, after he has paid his stock subscription, is liable personally for any part of the debts of the corporation. The [savings institution here involved], according to the evidence, in 1870 had a capital of fifty thousand dollars, yet the depositors lost about three hundred thousand dollars, six times as much as the whole capital stock. This corporation, by its directors, was by law permitted to carry on business, receive deposits, etc., and its stockholders would have reaped all the profits after the debts were paid, and yet are not personally liable for the debts of the corporation. The corporation has conferred upon it a privilege, which the natural person does not possess; and the modern authorities, recognizing this distinction and the great necessity for strict management of its affairs, have declared that its assets are a trust fund for the payment of creditors. Some of the authorities declare that the capital stock is a trust fund for the payment of the debts of the creditors. If the capital stock is, then why not that which represents the capital stock? Fifty thousand dollars, say, is paid in as the stock subscription. This money is loaned and bills and notes taken therefor. The fifty thousand dollars in cash is gone, but there is its equivalent with its accumulated earnings. If the capital stock is a trust fund for the payment of the debts of the corporation, then, I think, all the assets of the corporation are a trust fund for the same purpose. Why should this not be true? It is a very old doctrine, as old as corporations themselves, that the stockholders are not entitled to receive anything from the corporation until its debts are paid. If that is so, it seems to me it follows that the creditors are entitled to all the assets of the corporation, if necessary, for the payment of their debts. But if the assets of a corporation are a trust fund for the payment of the debts, who holds the property in trust? The directors are the managers of the corporation, and it has long been held that they are trustees for the corporation and its stockholders. They are to prudently and faithfully manage the affairs of the corporation, pay its debts, and divide the residue among the stockholders. They must necessarily look after the debts before they can discharge their trusts to the stockholders. If the assets are a trust fund for the payment of the debts of the corporation, it necessarily follows that the direct-

ors, in whose hands are those funds, are the trustees for the creditors of the corporation. When the directors of a banking corporation ascertain that it is hopelessly insolvent, so that individually they are unwilling longer to aid it, their manifest duty is to close its doors at once, for continuing to do business then (as receiving deposits) is a fraud upon the public, and they should not receive any more deposits nor pay any more checks, but should proceed to execute their trust, either by making a general assignment for the benefit of creditors, or by paying *pro rata* the debts of the corporation. Whether the board of directors could then, under peculiar circumstances, make preference of creditors, as was done in Burr *v.* McDonald, 3 Gratt. 216, it is unnecessary to decide in this case. But the directors had no right, occupying the fiduciary relation to the creditors generally which they did, to keep the doors of the [savings institution] open, until they could get out their deposits, and all the time from the 21st of February, 1871, until the 25th of the said month, luring depositors to give credit to the insolvent concern, while some of them, at least, including the defendant in this cause, were receiving their money from deposits thus improperly received. Before [defendant] received his money, the directors, under the evidence in this cause, should have closed the doors of the institution. Under these circumstances he had no right to draw his money, and thus prefer himself to the other creditors, for whom he was acting as trustee. To do so was a gross breach of trust and was also fraud."[1] The

[1] Lamb, Trustee, *v.* Laughlin, (1884) 25 W. Va. 300, 321, 322. The cases to sustain the director's position reviewed were Poole, Jackson & Whyte's Case, 9 Ch. Div. 322; Dana *v.* U. S. Bank, 5 Watts & Serg. 223; Catlin *v.* Eagle Bank, 6 Conn. 233; Pondville Co. *v.* Clark, 25 Conn. 97; Smith *v.* Skeary, 47 Conn. 47; Whitwell *v.* Warner, 20 Vt. 425; Stratton *v.* Allen, 1 C. E. Green (N. J.), 232; Daniels *v.* Davison, 16 Ves. 249; Moore *v.* Butler, 1 Scho. & Lef. 262; Railroad *v.* Claghorn, 1 Speers Eq. 562; Buell *v.* Buckingham, 16 Iowa, 291; Merrick *v.* Peru Coal Co., 61 Ill. 472; Burr *v.* McDonald, 3 Gratt. 216; Addison *v.* Lewis, 75 Va. 720; Planters' Bank *v.* Whittle, 78 Va. 737. The cases to the contrary were Wood *v.* Dummer, 3 Mason, 308; Curran *v.* Arkansas, 15 How. 308; Drury *v.* Cross, 7 Wall. 302; Koehler *v.* Black River Falls Iron Co., 2 Black, 720; Sawyer *v.* Hoag, 17 Wall. 610; Upton *v.* Tribilcock, 91 U. S. 47; Jackson *v.* Ludeling, 21 Wall. 616; County of Morgan *v.* Allen, 103 U. S. 498; Shea *v.* Mabry, 1 Lea (Tenn.), 319; Hastings *v.* Drew, 76 N. Y. 9; Goodin *v.* Canal Co., 18 Ohio St. 182; Richards *v.* Insurance Co., 43 N. H. 263; Colby *v.* Copp, 35 N. H. 434; Jones, McDowell & Co. *v.* Arkansas Mechanical & Agricultural Co., 38 Ark. 17; Bradley *v.* Farwell, 1 Holmes, 433; Coons & Braine *v.* Tome, 9 Fed. Rep. 532.

Supreme Court of the United States, in a late case, after a reference to cases which had been determined by that court, has said: "These cases negative the idea of any direct trust or lien attaching to the property of a corporation in favor of its creditors, and at the same time are entirely consistent with those cases in which the assets of a corporation are spoken of as a trust fund, using the term in the sense that we have said it was used. The same idea of equitable lien and trust exists in the case of partnership property. Whenever, a partnership becoming insolvent, a court of equity takes possession of its property, it recognizes the fact that in equity the partnership creditors have a right to payment out of those funds in preference to individual creditors, as well as superior to any claims of the partners themselves. And the partnership property is, therefore, sometimes said, not inaptly, to be held in trust for the partnership creditors, or that they have an equitable lien on such property. Yet all that is meant by such expressions is the existence of an equitable right which will be enforced whenever a court of equity, at the instance of a proper party, and in a proper proceeding, has taken possession of the assets. It is never understood that there is a specific lien, or a direct trust. A party may deal with a corporation in respect to its property as with an individual owner, and with no greater danger of being held to have received into his possession property burdened with a trust or lien. The officers of a corporation act in a fiduciary capacity in respect to its property in their hands, and may be called to an account for fraud or sometimes even mere mismanagement in respect thereto; but as between itself and its creditors, the corporation is simply a debtor, and does not hold its property in trust, or subject to a lien in their favor, in any other sense than does an individual debtor. That is certainly the general rule, and if there be any exceptions thereto, they are not presented by any of the facts in this case. Neither the insolvency of the corporation, nor the execution of an illegal trust deed, nor the failure to collect in full all stock subscriptions, nor all together, gave to these simple contract creditors any lien upon the property of the corporation, nor charged any direct trust thereon."[1] In a late case before the

[1] Hollins *v.* Brierfield Coal & Iron Co., (1893) 150 U. S. 371. They referred to the cases in these words: "In the case of The Wabash, St. Louis & Pacific Railway *v.* Ham, 114 U. S. 587, it appeared that four railway corporations owing debts were consolidated under authority of law,

Supreme Court of Nebraska that court held that the relation of the directors and managing officers of an insolvent private corporation towards the property and assets thereof is that of trustees for all of the creditors, and such officers cannot take advantage of their position to secure a preference for themselves, but are required to share ratably with other creditors.[1]

and by the terms of the consolidation agreement the new corporation was to protect the debts of the old. Subsequently the new corporation executed a mortgage on all its property, and in a contest between the mortgagees and the unsecured creditors of one of the constituent companies the court held that the lien of the mortgagees was prior. In respect to this, Mr. Justice GRAY (p. 594) thus stated the law: 'It was contended that the property of the Toledo and Wabash Railway Company was a trust fund for all its creditors, and that upon the consolidation the Toledo, Wabash and Western Railway Company took the property of the Toledo and Wabash Railway Company charged with the payment of all its debts. The property of a corporation is doubtless a trust fund for the payment of its debts, in the sense that when the corporation is lawfully dissolved and all its business wound up, or when it is insolvent, all its creditors are entitled in equity to have their debts paid out of its corporate property before any distribution thereof among the stockholders. It is also true in the case of a corporation as in that of a natural person that any conveyance of property of the debtor, without authority of law and in fraud of existing creditors, is void as against them.' The case of Fogg *v.* Blair, 133 U. S. 534, 541, presented a similar question, and this court, by Mr. Justice FIELD, observed: 'We do not question the general doctrine invoked by the appellant that the property of a railroad company is a trust fund for the payment of its debts, but we do not percive any place for its application here. That doctrine only means that the property must first be appropriated to the payment of the debts of the company before any portion of it can be distributed to the stockholders; it does not mean that the property is so affected by the indebtedness of the company that it cannot be sold, transferred or mortgaged to *bona fide* purchasers for a valuable consideration, except subject to the liability of being appropriated to pay that indebtedness. Such a doctrine has no existence.' In the case of Hawkins *v.* Glenn, 131 U. S. 319, 332, which was an action brought by the trustee of a corporation against certain of its stockholders to recover unpaid subscriptions, and in which the defense of the Statute of Limitations was pleaded, Chief Justice FULLER referred to this matter in these words: 'Unpaid subscriptions are assets, but have frequently been treated by courts of equity as if impressed with a trust *sub modo* upon the view that, the corporation being insolvent, the existence of creditors subjects liabilities to the rules applicable to funds to be accounted for as held in trust, and that, therefore, statutes of limitations do not commence to run in respect to them until the retention of the money has become adverse by a refusal to pay upon due requisition.'" See further on this subject Ford *v.* Plankinton Bank, (Wis. 1894) 58 N. W. Rep. 766, and an article by Seymour D. Thompson, one of the judges of the Court of Appeals of St. Louis, in 27 Am. Law Rev. 846.

[1] Ingwersen *v.* Edgecombe, (Neb. 1894) 60 N. W. Rep. 1032. The court considered the weight of authority as

§ 522. The power of directors of a corporation to execute an assignment of the corporation's property for the benefit of creditors.—The Supreme Court of Missouri has held that a private corporation, having the power to make an assignment for the benefit of creditors, and the management of its affairs being vested in the directors without restriction, the directors, and they alone, are authorized to make it; that when the corporation becomes crippled and unable to meet its obligations in the usual course of business it is the duty of the directors to care for the creditors, and it is competent for the directors to make an assignment, and this they may do without the consent of the stockholders.[1]

to the relation of the trustees to be in favor of the statement in the text, and cited in support of their judgment Haywood *v.* Lumber Co., 64 Wis. 639; s. c., 26 N. W. Rep. 184; Hopkins' Appeal, 90 Pa. St. 69; Sieardi *v.* Oil Co., 149 Pa. St. 139; s. c., 24 Atl. Rep. 163; Olney *v.* Land Co., 16 R. I. 597; s. c., 18 Atl. Rep. 181; Rouse *v.* Bank, 46 Ohio St. 493; s. c., 22 N. E. Rep. 293; Hays *v.* Bank, 51 Kans. 535; s. c., 33 Pac. Rep. 318; Thompson *v.* Lumber Co., 4 Wash. St. 600; s. c., 30 Pac. Rep. 741, and 31 Pac. Rep. 25; Corey *v.* Wadsworth, (Ala.) 11 So. Rep. 350; Adams *v.* Milling Co., 35 Fed. Rep. 433; 2 Dillon Mun. Corp. 787, 803; Beach Priv. Corp. 241 et seq.; Wait Insol. Corp. 162. As to the doctrine of the assets of a corporation being a trust fund for its creditors, see Alberger *v.* National Bank of Commerce, 123 Mo. 313; s. c., 27 S. W. Rep. 657; Fear *v.* Bartlett, (Md.) 32 Atl. Rep. 322; O'Bear Jewelry Co. *v.* Volfer, (Ala.) 17 So. Rep. 525, overruling Corey *v.* Wadsworth, 99 Ala. 68; s. c., 11 So. Rep. 350; Goodyear Rubber Co. *v.* George D. Scott Co., 96 Ala. 439; s. c., 11 So. Rep. 370, and Gibson *v.* Furniture Co., 96 Ala. 357; s. c., 11 So. Rep. 365. See, also, Worthen *v.* Griffith. 59 Ark. 562; s. c., 28 S. W. Rep. 286; Chattanooga, R. & C. R. Co. *v.* Evans, 14 C. C. A. 116; s. c., 66 Fed. Rep. 809.

[1] Hutchinson *v.* Green, (1886) 91 Mo. 367, 375; s. c., 1 S. W. Rep. 853. The court cited Chew *v.* Ellingwood, 86 Mo. 260; Dana *v.* The Bank of the United States, 5 W. & S. 223; De Camp *v.* Alward, 52 Ind. 473, in support of this conclusion. The court said: "The directors may with propriety consult with the stockholders, but under the circumstances just stated, and in the exercise of their best judgment, they may make the assignment even against the expressed will of the stockholders. Of the cases relied upon by the [stockholders attacking this assignment] that of Abbott *v.* American Hard Rubber Co., 33 Barb. 580, was not an assignment for the benefit of creditors. There the trustees attempted, through the form of a sale, to secure to themselves the property of the corporation at the expense of the other stockholders. The sale was voidable as to the stockholders not consenting, although a majority agreed to the transaction. No question of the validity of a voluntary assignment of an insolvent corporation made for the benefit of creditors was involved in the case. The same may be said of Northern Railroad *v.* Concord Railroad, 50 N. H. 175, for there the purpose of the contract brought in

§ 523. **Preferences of creditors by insolvent corporation.** — The right of a railroad company in this case to make preferences among its creditors was brought in question. The United States Circuit Court for the eastern district of Arkansas held that under the decisions of the courts of Arkansas, and at common law, an insolvent corporation may make preferences among its creditors in good faith, so long as its right to do so is not restrained by statute.[1] A corporation in failing circumstances

question was to transfer the management of the affairs of one company to the other for a period of five years. The assignment was upheld in Eppright *v.* Nickerson, 78 Mo. 482, though the stockholders did not authorize or assent to it. In that case the assignment was not assailed by any stockholder, and the court, by way of concession, made some remarks which seem to imply that consent on the part of the stockholders was essential to give validity to an assignment as against them, but of these remarks enough was said in Chew *v.* Ellingwood, 86 Mo. 260." As to the power of a corporation to make an assignment for the benefit of creditors, see Shockley *v.* Fisher, 75 Mo. 498. As to assignments for benefit of creditors, see In re Lehigh Co.'s Estate, 12 Pa. Co. Ct. Rep. 257; National Bank of Commerce *v.* Shumway, 49 Kans. 224; Potts *v.* Wallace, 146 U. S. 689; s. c., 13 Sup. Ct. Rep. 196; Vanderpoel *v.* Gorman, 22 N. Y. Supp. 541.

[1] Gould *v.* Little Rock, M. R. & T. Ry. Co., (1892) 52 Fed. Rep. 680; citing Ex parte Conway, 4 Ark. 302, 348, 354; Ringo *v.* Biscoe, 13 Ark. 563. CALDWELL, Circuit Judge, said: "The established rule in [Arkansas] is in harmony with the general, though not quite uniform, current of authorities in this country on the question. 2 Mor. Corp. § 802; Allis *v.* Jones, 45 Fed. Rep. 148; Covert *v.* Rogers, 38 Mich. 363; Coats *v.* Donnell, 94 N. Y. 168; Dana *v.* Bank, 5 Watts & S. 223; Warner *v.* Mower, 11 Vt. 390; Whitwell *v.* Warner, 20 Vt. 426; Stratton *v.* Allen, 16 N. J. Eq. 229; Wilkinson *v.* Bauerle, 41 N. J. Eq. 635; s. c., 7 Atl. Rep. 514; Duncomb *v.* Railroad Co., 84 N. Y. 190; 88 N. Y. 1; Harts *v.* Brown, 77 Ill. 226; Reichwald *v.* Hotel Co., 106 Ill. 439; Buell *v.* Buckingham, 16 Iowa, 284 (opinion by Judge DILLON); Hallam *v.* Hotel Co., 56 Iowa, 178; s. c., 9 N. W. Rep. 111; Garrett *v.* Plow Co., 70 Iowa, 697; s. c., 29 N. W. Rep. 395; Smith *v.* Skeary, 47 Conn. 47; Bank *v.* Whittle, 78 Va. 737; Ashhurst's Appeal, 60 Pa. St. 314; Sargent *v.* Webster, 13 Met. 497." Then he discusses the question generally: "In some states, by statute, the property of an insolvent corporation must be devoted to the payment *pro rata* of all its creditors, and, after the insolvency of the corporation is known, the directors cannot divert its property from such use by giving preferences to some of its creditors; but where there is no such statute the great weight of authority is that the property of an insolvent corporation may be held and used by its directors in the payment of some of its creditors to the exclusion of others. Its insolvency does not affect its right to make preference any more than the right of an individual debtor to make preferences is affected by his insolvency. The cases which hold the contrary doctrine are bottomed on the erroneous theory that the insolvency of a corporation, in effect, dissolves it, and makes

may, in Missouri, prefer one creditor to another in discharging its obligations, if such preference is made in good faith, while the property of the corporation remains in its possession and unaffected by liens or by process of law. Such a preference is not invalidated by the subsequent act of the failing corporation in making a general assignment on the same day for the benefit of its creditors. Nor is such a preference rendered fraudulent because the amount of property transferred is largely in excess of the

the directors mere trustees to distribute its assets ratably among its creditors. It is undoubtedly true that the property of a corporation is in one sense a trust fund for the payment of its debts; but this rule means no more than that the property of a corporation cannot be distributed among its stockholders, or applied to any purpose foreign to the legitimate business of the corporation until its debts are paid. The rule, so far as it relates to the payment of debts, is satisfied whenever the property of a corporation is applied to the payment of any of its *bona fide* debts. The rule, as has been often pointed out, does not prevent a corporation, whether solvent or insolvent, from making preferences among its creditors, and exercising in good faith absolute dominion over its property in the conduct of its legitimate corporate business, so long as its right to do so is not restrained by statute or by judicial proceedings. In Fogg *v.* Blair, 133 U. S. 534, 541; s. c., 10 Sup. Ct. Rep. 338, Mr. Justice FIELD, in delivering the opinion of the court, calls attention to the fact that the property of a corporation is not a trust fund for creditors in any other sense than we have stated. He says: 'We do not question the general doctrine invoked by the appellant that the property of a railroad company is a trust fund for the payment of its debts, but do not perceive any place for its application here. That doctrine only means that the property must first be appropriated to the payment of the debts of the company before any portion of it can be distributed to the stockholders. It does not mean that the property is so affected by the indebtedness of the company that it cannot be sold, transferred or mortgaged to *bona fide* purchasers for a valuable consideration, except subject to the liability to be appropriated to pay that indebtedness. Such a doctrine has no existence. The cases of Curran *v.* State, 15 How. 304, 307, and Wood *v.* Dummer, 3 Mason, 308, give no countenance to anything of this kind.' The case of Rouse *v.* Bank, 46 Ohio St. 493; s. c., 22 N. E. Rep. 293, is cited in support of the proposition that the property of an insolvent corporation is a trust fund for its creditors in a sense that precludes the corporation from making preferences among its creditors or otherwise using its property in the conduct of its corporate business. Referring to the doctrine of this case, the Supreme Court of the United States, speaking by Mr. Justice GRAY, says: 'That decision, it is true, proceeded in part upon the theory that the property of an insolvent corporation is a trust fund for its creditors in a wider and more general sense than could be maintained upon general principles of equity jurisprudence. Graham *v.* Railroad Co., 102 U. S. 148, 161; Railroad Co. *v.* Ham, 114 U. S. 587, 594; s. c., 5 Sup. Ct. Rep. 1081; Richardson's Exrs. *v.* Green, 133 U. S. 30, 44; s. c., 10 Sup. Ct. Rep. 280;

debt thereby preferred.[1] They held also that the mere insolvency of a corporation does not of itself transform its assets into a trust fund for the equal benefit of all creditors.[2] The Illinois Supreme Court has declared the settled law of that state to be that corporations may prefer creditors; that the corporate property of the corporations is not held in trust in such sense as to forbid the corporation from giving judgment notes, confessions of judgments or mortgages, or doing any other matter or thing in the exercise of the right they have to prefer one creditor to another. As to what is required of the officers of the corporation in such transactions, they declared the rule to be that the persons to whom the corporation intrusts the exercise of its right to prefer creditors, must exercise the trust in the utmost good faith, without regard to the extent of their personal interest in the corporation or its property; and that the fact that the corporation may be embarrassed with debts, or may be well nigh or wholly insolvent, will not lessen the duty to exercise with fairness the power given them. The officers, as they represent the corporation, have no right to join creditors or stockholders hostile to the corporation

Fogg *v.* Blair, 133 U. S. 534, 541; s. c., 10 Sup. Ct. Rep. 338; Peters *v.* Bain, 133 U. S. 670, 691, 692; s. c., 10 Sup. Ct. Rep. 354;' Purifier Co. *v.* McGroarty, 136 U. S. 237; s. c., 10 Sup. Ct. Rep. 1017. A good many courts have from time to time inveighed against the rule of the common law which allows a debtor to make preferences among his creditors, but the rule is too firmly imbedded in our system of jurisprudence to be overthrown by judicial decision, and it can no more be overthrown by the courts in its application to corporations than to individuals. In Wilkinson *v.* Bauerle, 41 N. J. Eq. 635; s. c., 7 Atl. Rep. 514, the court said: 'Both reason and authority establish the proposition that a corporation may sell and transfer its property, and may prefer its creditors, although it is insolvent, unless such conduct is prohibited by law.' We think this is a correct statement of the rule, and that it can only be abrogated by legislation."

[1] Alberger *v.* National Bank of Commerce, (Mo. 1894) 27 S. W. Rep. 657. Upon the second point the court cited Union Bank *v.* Kansas City Bank, (1889) 136 U. S. 223; s. c., 10 Sup. Ct. Rep. 1013. As to the second, Hargadine *v.* Henderson, (1888) 97 Mo. 375; s. c., 11 S. W. Rep. 218; Jaffray *v.* Mathews, (Mo. 1894) 25 S. W. Rep. 187.

[2] Alberger *v.* National Bank of Commerce, (Mo. 1894) 27 S. W. Rep. 657, following La Grange Butter Tub Co. *v.* National Bank of Commerce, (Mo. 1894) 26 S. W. Rep. 710. On the subject of preferences of creditors by a corporation the court cited City of St. Louis *v.* Alexander, (1856) 23 Mo. 524, which was approved in Kitchen *v.* Railway Co., (1878) 69 Mo. 254, and in Foster *v.* Planing Mill Co., (1887) 92 Mo. 87; s. c., 4 S. W. Rep. 260. They distinguished Rouse *v.* Bank, (1889) 46 Ohio St. 493; s. c., 22 N. E. Rep. 293; Lyons-Thomas Hardware Co. *v.* Perry Stove Manufg. Co., (Tex. Sup. 1893) 24 S. W. Rep. 16.

in hostile action to the corporation or its property. They must always act in the interest of the corporation, and adversely to the enemies seeking to destroy the corporation.[1] In Pennsylvania an insolvent corporation may prefer a creditor by a confession of judgment.[2] And a sale under a judgment confessed by an insolvent corporation will not be restrained by a court of equity on the ground that a sale of the corporation's property can be more advantageously conducted in the interests of all the creditors by receivers. For until the rights of the other creditors are violated no one has standing to challenge the execution creditor's rights to use the means provided by law for the enforcement of his claim.[3] The corporation here was a foreign one, organized under the laws of New Jersey, and it was attempted to apply the laws of that state to the case. But the court held that where no disability to make a preference of one creditor before another was imposed upon a foreign corporation by its charter, the prohibition of such a preference by a general enactment of the state where the corporation was chartered could have no extraterritorial effect.[4] In an action for the foreclosure of a chattel mortgage executed by a corporation to secure the claims of certain creditors, it appeared that the corporation afterwards made a general assignment for the benefit of its creditors. The Supreme Court of Michigan declared the rule in that state to be that it is not unlawful for a corporation, though insolvent, to give preferences to its creditors by way of mortgage.[5] A corporation in failing

[1] J. W. Butler Paper Co. *v.* Robbins, (1894) 151 Ill. 588.

[2] Pairpoint Mfg. Co. *v.* Phila. Optical & Watch Co., (1894) 161 Pa. St. 17, following Lake Shore Banking Co. *v.* Fuller, 110 Pa. St. 156.

[3] Pairpoint Mfg. Co. *v.* Phila. Optical & Watch Co., (1894) 161 Pa. St. 17. See, also, Lowry, Trustee, etc., *v.* Phila. Optical & Watch Co., (1894) 161 Pa. St. 123.

[4] Pairpoint Mfg. Co. *v.* Phila. Optical & Watch Co., (1894) 161 Pa. St. 17. As to corporations preferring creditors by assignment in Illinois, and that the law of the state where incorporated has no effect to prevent it, see Warren *v.* First National Bank of Columbus, (1893) 149 Ill. 9.

[5] Bank of Montreal *v.* J. E. Potts Salt & Lumber Co., (1892) 90 Mich. 345; citing Kendall *v.* Bishop, 76 Mich. 634, and others. The court referred to certain cases in that state in these words: "In the case of Town *v.* Bank, 2 Doug. (Mich.) 530, certain creditors were preferred by the corporation in a common-law assignment. It was held that the corporation had the same right to prefer one creditor over another that an individual has. In Turnbull *v.* Lumber Co., 55 Mich. 396, it appeared that the corporation was converting its assets into money as rapidly as possible and paying only certain of the creditors. The corporation was at the time insolvent." Speaking of these acts of the corpo-

circumstances cannot borrow money with which to purchase shares in itself, and give to the person from whom the loan is made a preference over all other creditors by confessing judgments, when insolvent, in favor of the persons loaning the money with actual knowledge of the purpose for which the same was borrowed, when such conduct works a fraud upon *bona fide* creditors, and defeats the collection of their claims.[1] In case an insol-

ration, Mr. Justice CHAMPLIN said: "It being insolvent such action must result in the payment of some to the exclusion of others. Such conduct * * * although legal and proper before a bill is filed against it by a judgment creditor whose execution is returned unsatisfied, becomes improper after the filing of such bill. From that time on no unsecured creditor is entitled to a preference over others. In the case of Hills *v.* Furniture Co., 23 Fed. Rep. 434, a mortgage had been given by an insolvent corporation to secure certain creditors. It was said: 'It does not affect the question if the company could never pay its debts in full, for the legal right of an insolvent debtor to secure one or more creditors, in preference to others, where no fraud is intended, is settled in Michigan by many decisions.'"

[1] Adams & Westlake Co. *v.* Deyette, (S. D. 1894) 59 N. W. Rep. 214. The court, discussing the subject generally, said: "The property and capital of a corporation gives it financial standing, because it is primarily liable for its debts. Persons extending credit to such corporations do so upon the faith that its officers and agents will conduct its affairs in a manner consistent with business principles, and when such officers devote the corporate assets to their individual use and benefit to the exclusion of creditors courts without hesitation characterize such acts, as to creditors, fraudulent and void. Independently of the question of actual fraud in the case under consideration, the immediate effect of the purchase of the Trask stock at a time when the corporation was financially embarrassed, if not, indeed, insolvent, was to increase its liability, without adding anything to its resources to which plaintiff could look for the security or payment of its claim, and such conduct is contrary to the spirit, if not the letter, of our statute, and is not upheld by the courts. Comp. Laws Dak. §§ 2917, 2928. In Currier *v.* Slate Co., 56 N. H. 262, the court says: 'The funds of an insolvent corporation cannot be taken to buy a portion of its capital stock. * * * It would be grossly inequitable to the other stockholders, and a fraud upon creditors.' From Coppin *v.* Greenlees, 38 Ohio St. 275, we quote the following: 'The doctrine that corporations, when not prohibited by their charter, may buy and sell their own stock, is supported by a line of authorities, but nevertheless we think the decided weight of authority, both in England and the United States, is against the exercise of the power, unless conferred by an express grant or clear implication. * * * It is true, however, that in most jurisdictions where the right of a corporation to traffic in its own stock has been denied, an exception to the rule has been admitted to exist whereby a corporation has been allowed to take its own stock in satisfaction of a debt due it. This exception is supposed to rest upon a necessity which arises in order to avoid loss.' If a corporation to the injury of creditors can borrow money for the purchase of one share

vent corporation assigns all its property to one of its creditors for the purpose of satisfying its debt to that creditor, the remedy of the other creditors wishing to attack the assignment is by suit in equity to compel an equal distribution of the corporate assets.[1] A chattel mortgage executed by the president and secretary of an insolvent corporation, with the knowledge and consent of all the stockholders, has been held to be valid by the Supreme Court of Michigan.[1] The Supreme Court of Illinois has held that the general statute of New York prohibiting the assignment or transfer of property in contemplation of insolvency had no application to an assignment of a fund in Illinois executed in Ohio by a New York corporation.[2]

§ 524. **Attachment of property of insolvent corporation — the right of a creditor to attach — lien of the attachment, etc.** — A Colorado corporation, a land company, in proceedings in insolvency to wind it up and obtain an equitable distribution of its assets, was placed in the hands of a receiver, and the receivership was extended to lands in another state. The United States Circuit Court of Appeals for the eighth circuit held that the court of equity which had appointed this receiver had no

of its stock, or the stock held by one member, it can borrow money with which to purchase the shares of all its members and thus destroy its very existence, as no corporation like the defendant can have an existence in this jurisdiction without stock and without stockholders. The doctrine is well established that a purchase of shares in itself by a corporation is against public policy and *ultra vires*, whenever such purchase diminishes its ability to pay its debts or lessens the security of its creditors. Bank *v.* Wulfekuhler, 19 Kans. 60; Gill *v.* Balis, 72 Mo. 424; Barton *v.* Plank Road Co., 17 Barb. 397; Clapp *v.* Peterson, 104 Ill. 26; 1 Spell. Priv. Corp. 168, and cases there cited."

[1] Holbrook, Merrill & Stetson *v.* Peters & Miller Co., (Wash. 1894) 36 Pac. Rep. 256. For a case holding that a corporation which has ceased to do business, or by conveying its property to a trustee for the benefit of its creditors incapacitated itself for continuing business, having no power to prefer its creditors, see Lyons-Thomas Hardware Co. *v.* Perry Stove Manuf. Co., (Tex. 1894) 27 S. W. Rep. 100.

[1] Kalamazoo Spring & Axle Co. *v.* Winans, Pratt & Co., (Mich. 1895) 64 N. W. Rep. 23.

[2] Warren *v.* First National Bank, (Ill. 1895) 38 N. E. Rep. 122. Transfers of property of insolvent corporations have been held to be void in Brouwer *v.* Harbeck, 9 N.Y. 589 That a deed of assignment made by a corporation under the insolvency laws of Minnesota, regular and complete on its face, cannot be collaterally attacked, see Staples *v.* Schulenberg & Boeckeler Lumber Co., (Minn. 1895) 64 N. W. Rep. 148, following Bank *v.* Schranck, 43 Minn. 38; s. c., 44 N. W. Rep. 524.

power to enjoin a citizen of the other state or jurisdiction from levying an attachment on the lands in that state, unless he was a party, either in person or by representation, in the proceedings in which the receiver was appointed; also, that a lien having been established by such an attachment suit, which neither the receiver nor the corporation's other creditors could divest, there was nothing to prevent a party to the receivership proceedings from taking an assignment of the judgment and lien, with all the rights of enforcement belonging to the original owner of the judgment. But the court had authority to enjoin one who had joined in the receivership proceedings and had been active in extending the receivership to the lands in the other state, and afterwards caused suit to be brought in that other state, to collect a debt and thereby obtained a lien on the lands, from enforcing the lien or in any way interfering with the receiver's possession or disposition of the property.[1] Valid attachments of the property of a corporation, made before the filing of a bill for the appointment of a receiver for the corporation, are not dissolved by the filing of such bill and the subsequent appointment of a receiver.[2] The Missouri Supreme Court has in a late case held that, though a corporation is insolvent, a creditor not connected with the corporation may obtain preference, before a court of equity obtains jurisdiction over it for winding up its affairs, by attaching the property of the corporation, though he is advised so to do by a director of the corporation.[3] The Iowa Supreme Court has held

[1] Schindelholz *v.* Cullum, (1893) 55 Fed. Rep. 885. As to property in the hands of a receiver of an insolvent corporation being exempt from being interfered with by an officer under process issued in other cases, see Harrison *v.* Waterberry, (Tex. 1894) 27 S. W. Rep. 109.

[2] Page *v.* Supreme Lodge Knights & Ladies of Protection, (Mass. 1894) 37 N. E. Rep. 369; citing Atlas Bank *v.* Nahant Bank, 23 Pick. 480; Kilborne *v.* Lyman, 6 Met. 299; Hubbard *v.* Bank, 7 Met. 346; Davenport *v.* Tilton, 10 Met. 325; Hills *v.* Parker, 111 Mass. 510; Book Co. *v.* De Golyer, 115 Mass. 69; Sage *v.* Heller, 124 Mass. 213; Garham *v.* Mutual Aid Society, (Mass. 1894) 37 N. E. Rep. 447; Taylor *v.* Insurance Co., 14 Allen, 353; Folger *v.* Insurance Co., 99 Mass. 267; Burdon *v.* Association, 147 Mass. 360; s. c., 17 N. E. Rep. 874.

[3] La Grange Butter Tub Co. *v.* National Bank of Commerce, (Mo. 1894) 26 S. W. Rep. 710. The court declare the principles of law ruling in Missouri courts, in such cases, in these words: "While it may be conceded that corporate assets are regarded as a trust fund for the benefit of all the corporation creditors, the rule, as announced by this court in Foster *v.* Planing Mill Co., 92 Mo. 79; s. c., 4 S. W. Rep. 260, is that a corporation may, when acting within the scope of the pur-

that an officer of a corporation, who is also its creditor, may attach its property for the collection of his debt, though he knows of its failing circumstances, but is in no way responsible therefor, and though he knows that his attachment will precipitate a crisis in its affairs; and his attachment will be good as against subsequent attaching creditors and mortgagees.[1] Corporations, it has been held in Maryland, are not subjected to the insolvency laws of that state.[2] The property of this corporation was sold by the officers of the federal court at the end of an attachment proceeding. The title of the purchaser was attacked in this action upon the officers' bond. The purpose of the writ of error to the United States Circuit Court of Appeals for the eighth circuit was to present the question whether a business corporation, when it became insolvent, thereafter held all of its property in trust for equal distribution among its creditors, and was deprived of the common-law power of preferring creditors, which individuals ordinarily possessed. The court, on account of the record not presenting it properly, did not determine it. But they did not hold that, if the theory that corporate property is a trust fund for its creditors is invoked to invalidate a conveyance which operates a preference, there was no reason why it should not also operate to prevent complaining creditors from obtaining priority by an attachment. And in this case, the purchaser, in good faith, for full value, without notice of defects in the seller's title, it was held could hold property, as against an attaching creditor of the corporation from

poses for which it was incorporated, do any act in furtherance of those purposes, and, although insolvent, it may prefer some creditors to others, even though such creditors be among the directors of the corporation, provided such preference is made in good faith, and to a *bona fide* creditor. This rule only applies to the acts of the corporation while it is a going concern, and before it has gone into the hands of a receiver, or liens have attached to the corporate property. It is true, as held in Roan *v.* Winn, 93 Mo. 503; s. c., 4 S. W. Rep. 736, and authorities cited, that, after confessed insolvency, the directors of a corporation cannot, in equity, secure any advantages to themselves. This is because they represent all the creditors, and occupy the position of trustees towards them, and a trustee, or a person standing in a similar or fiduciary relation, will not, in equity, be allowed to take advantage of his position, exercise his power, or to manage or appropriate the property of which he has the control, for his own profit and to his own advantage, at the expense of those for whom he is acting."

[1] Rollins *v.* Shaver Wagon & Carriage Co., (1890) 80 Iowa, 380; s. c., 45 N. W. Rep. 1037.

[2] Ellicott Machine Co. *v.* Speed, (1889) 72 Md. 22; s. c., *sub nom.* Search *v.* Ellicott, 18 Atl. Rep. 863.

which the seller obtained it, even if the seller had notice of the insolvency of the corporation, and his title would have been invalidated thereby.[1] In case the property of an insolvent foreign corporation has been seized by the sheriff under a warrant of attachment issued by a state court in an action afterwards prosecuted to judgment, an execution issued and levy made upon the property seized, a receiver of such corporation, appointed subsequent to the attachment by the United States Circuit Court of the district where such property is situated, takes the property of the corporation in that jurisdiction, subject to such rights over the same as had been acquired by the various proceedings in the state court.[2] Where funds attached had been paid over to the receiver by order of the court, without prejudice to the rights of the attaching parties, it was held in Massachusetts that the receiver took the property subject to all valid attachments, to the extent of the property lawfully attached before the filing of a bill for a receiver, the claims of the attaching creditors, if allowed to be proved, must be treated as preferred.[3] It has been held by the Court of Civil Appeals of Texas, on a rehearing, that a creditor of an insolvent corporation, obtaining a lien by judicial process on the assets of the corporation, may have the assets applied to the payment of his claim, to the exclusion of other creditors.[4]

[1] Walker *v.* Miller, (1894) 59 Fed. Rep. 869. See Hollins *v.* Iron Co., 150 U. S. 371; s. c., 14 Sup. Ct. Rep. 127; Brown *v.* Furniture Co., 58 Fed. Rep. 286, 292; s. c., 7 C. C. A. 225.

[2] Cole *v.* Oil Well Supply Co., (1893) 57 Fed. Rep. 534.

[3] Page *v.* Supreme Lodge Knights & Ladies of Protection, (Mass. 1894) 37 N. E. Rep. 369; citing Walling *v.* Miller, 108 N. Y. 173; s. c., 15 N. E. Rep. 65.

[4] Harrigan *v.* Quay, (Tex. Civ. App. 1894) 27 S. W. Rep. 897. This case, in the opinion of this court, rendered on appeal, in 26 S. W. Rep, 512, has been remanded so that the creditors of the insolvent corporation other than the one claiming that the assets should be applied first to his attachment, might raise the question whether the property of the insolvent corporation should be administered for the benefit of all the creditors, and that the one proceeding under the attachment was not entitled to any portion of it, except what might be his *pro rata* share of it as a creditor. On the hearing the court held that its former judgment was error, and said: "The rule of law that exists in this state that denies the right of an insolvent corporation, by contract, to transfer its property to a trustee for the benefit of preferred creditors, does not, in our opinion, interfere with the rights of a diligent creditor to pursue the remedies provided by law for the collection of his debt, and subjecting the property of such corporation to its payment. The fact that a corporation may be insolvent does not deprive the creditor of his right to sue it, and to levy upon its property to satisfy his judgment."

§ 525. **Receivers — rules as to appointment.**—The Court of Chancery of New Jersey, on a bill filed for appointment of a receiver for a corporation, has announced these rules: Nothing short of present actual insolvency will warrant the appointment of a receiver to wind up a corporation. Expected insolvency at some time in the future is not sufficient. A court of equity, in the exercise of its general jurisdiction, may appoint a receiver of a corporation, either because it has no properly constituted governing body or because there are such dissensions in its governing body as to make it impossible for the corporation to carry on its business with advantage to its stockholders; but this power is always exercised with great caution and only for such time and to such an extent as may be necessary to preserve the property of the corporation and to protect the rights of its stockholders.[1] The United States Circuit Court of Appeals for the fifth circuit affirmed the order appointing a receiver in this action by stockholders and bondholders and others, bondholders only, against an Alabama corporation, on the ground that the equities presented

That an attachment cannot be levied under the California rulings on the assets of a bank after the date of its insolvency, as decreed in the proceedings under the California Statutes, for winding up an insolvent bank's business, see Crane *v.* Pacific Bank, (Cal.) 39 Pac. Rep. 215.

[1] Edison *v.* Edison United Phonograph Co., (N. J. Eq. 1894) 29 Atl. Rep. 195. VAN FLEET, V. C., said: "This is the doctrine, as I understand it, which was laid down by Vice-Chancellor MALINS in Featherstone *v.* Cooke, L. R., 16 Eq. 298, and Auxiliary Co. *v.* Vickers, L. R., 16 Eq. 303, and which was approved by Chancellor RUNYON in Einstein *v.* Rosenfeld, 38 N. J. Eq. 309, and by Chancellor MCGILL in Archer *v.* Waterworks Co., 50 N. J. Eq. 33; s. c., 24 Atl. Rep. 508. But neither of the grounds which this doctrine recognizes as sufficient to warrant the appointment of a receiver exists in this case. The defendant corporation has a lawfully constituted governing body, which is in peaceable possession of all its property, controlling and directing its business regularly and peacefully, in conformity to the judgment of seven of its nine directors. Two of the nine differ in judgment from the other seven. The two believe that the adoption of a different course of business from that which is now proposed would result in larger gains. Both methods are clearly within the purposes and powers of the corporation. Which method shall be pursued, or whether one or both, is a question which the law commits absolutely and unconditionally to the judgment of a majority of the directors. Though somewhat disguised, the real purpose of the bill in this case appears, when critically examined, to be to induce judicial action which shall substitute the judgment of a minority of the directors of this corporation for that of the majority. That cannot be done. It is beyond judicial power. No rule of law is better settled than that which declares that so long as the directors of a corporation keep within

in the bill warranted the court to intervene for the preservation of the trust property. The allegations, among others, were that there was an issue of the bonds, when financially embarrassed, by the company, to the amount of $300,000, to raise more money, secured by a mortgage, the greater part of which bonds had been disposed of at or near par and the rest hypothecated for debts; that valuable properties of the corporation had been disposed of at ruinous rates to meet debts of the corporation; that the real estate had been sold for taxes; that default had been made upon the interest of the bonds; that the price of the bonds was depressed to a very low figure; that at a meeting presided over by its president, holding a majority of the proxies, few stockholders being present, it was voted to issue $1,000,000 in bonds; that the trustee had brought no suit to foreclose the mortgage made to secure the principal and interest of the bonds; that the management was wasteful and extravagant and entirely controlled by the president of the corporation.[1] The Supreme Court of Minnesota has held that in an action brought under the provisions of the General Statutes of 1878, chapter 76, for the purpose of sequestrating the property of an insolvent corporation and enforcing the constitutional liability of its stockholders, the plaintiff was not entitled, on the pleadings and as a matter of absolute right, to have a receiver appointed when it appeared that proceedings were pending under the Insolvency Law, in which a receiver or assignee had been designated or selected, who had qualified, and under the supervision of the court had entered upon and was dis-

the scope of their powers, and act in good faith and with honest motives, their acts are not subject to judicial control or revision. The statement of the principle of Vice-Chancellor GREEN in Ellerman *v.* Stock Yards Co., 49 N. J. Eq. 217, 232; s. c., 23 Atl. Rep. 287, is adopted by the court, and the same was restated by the same vice-chancellor in Sewell *v.* Beach Co., 50 N. J. Eq. 717, 723; s. c., 25 Atl. Rep. 929. Chancellor MCGILL, in Benedict *v.* Construction Co., 49 N. J. Eq. 23, 36; s. c., 23 Atl. Rep. 485, expressed it in these words: 'If stockholders in a corporation disapprove of the company's management, which is conducted without fraud, or by actions not *ultra vires*, or not in gross abuse of trust, or shall consider their speculation a bad one, their remedy is to elect new officers or sell their shares and withdraw. Where the question is one of mere discretion in the management of corporate business, or of doubtful event in the undertaking in which the corporation had embarked, remedy cannot be had by application to a court of equity.'"

[1] Fort Payne Coal & Iron Co. *v.* Sayles, (1893) 55 Fed. Rep. 360. As to appointment of receivers of insolvent corporations, see Straman *v.* North Baltimore Water Works Co., 8 Ohio Cir. Ct. Rep. 89; Ford *v.* Kansas

charging the duties of his trust.[1] Charges in a bill brought by one stockholder against a corporation and the other stockholders, that the president of the corporation refuses to account for money intrusted to him for the interests of the company, or to allow any

City & I. S. L. R. Co., 52 Mo. App. 439; Espuela Land & Cattle Co. *v.* Bindle, 5 Tex. Civ. App. 18; s. c., 23 S. W. Rep. 819; State *v.* Bank of New England, (Minn.) 56 N. W. Rep. 575; McGeorge *v.* Big Stone Gap Improvement Co., 57 Fed. Rep. 262; Porter *v.* Industrial Information Co., 5 Misc. Rep. 262; s. c., 25 N. Y. Supp. 328; Ralph *v.* Shiawassee Circuit Judge, (Mich.) 58 N. W. Rep. 837; Towle *v.* American Bldg., Loan & Inv. Soc., 60 Fed. Rep. 131; In re Lewis, 52 Kans. 660; s. c., 35 Pac. Rep. 287; Downing *v.* Dunlap Coal, Iron & Ry. Co., (Tenn.) 24 S. W. Rep. 122; Davis *v.* Power Co., 77 Md. 35; Lime City Building, Loan & Sav. Assn. *v.* Black, (Ind.) 35 N. E. Rep. 829; Supreme Sitting of the Order of Iron Hall *v.* Baker, (Ind.) 33 N. E. Rep. 1128; Fort Payne Furnace Co. *v.* Ft. Payne Coal & Iron Co., (Ala.) 11 So. Rep. 439; Showalter *v.* Improvement Co., 83 Tex. 162; Fluker *v.* Railway Co., 48 Kans. 577; Hinckley *v.* Pfister, 83 Wis. 64; s. c., 53 N. W. Rep. 21; Zieverink *v.* Kemper, (Ohio) 34 N. E. Rep. 250; Davis *v.* United States Electric Power & Light Co., (Md.) 25 Atl. Rep. 982; Merchants' Nat. Bank *v.* Manuf. Co., 48 Minn. 361. Effect of appointment upon an attachment. Waverly Co. *v.* Worthington Co., 24 N. Y. Supp. 331. Jurisdiction in such matters. Glines *v.* Supreme Sitting Order of Iron Hall, 22 Civ. Pro. Rep. 437; s. c., 20 N. Y. Supp. 275. Where the claims against a corporation were ascertained and small in comparison with the property sought to be sequestrated, and no notice of the application for a receiver under the statutes of Virginia had been given to the corporation, and an offer had been made to secure those claims should they be established by giving any bond that might be required, it was held that it was error to appoint such a receiver in Va., Tenn. & Car. Steel & Iron Co. *v.* Wilder, (1892) 88 Va. 942.

[1] Walther *v.* Seven Corners Bank, (Minn. 1894) 59 N. W. Rep. 1077. As to the power of a court in California to appoint a receiver for an insolvent bank, see People's Home Sav. Bank *v.* Court, 103 Cal. 27. As to power of bank commissioners in California in winding up an insolvent bank's affairs, see Long *v.* Court, 102 Cal. 449. When a receiver will be appointed for an insolvent corporation. Hale-Berry Co. *v.* Diamond State Iron Co., (Ga.) 22 S. E. Rep. 217; Mosher *v.* Supreme Sitting of Order of Iron Hall, 34 N. Y. Supp. 816; Security Savings & Trust Co. *v.* Piper, (Idaho) 40 Pac. Rep. 144; San Antonio & G. S. R. Co. *v.* Davis, (Tex. Civ. App.) 30 S. W. Rep. 693; Hatfield *v.* Cummings, (Ind.) 40 N. E. Rep. 53; Cotton Mills *v.* C. C. Randleman Cotton Mills, 115 N. C. 475; s. c., 20 S. E. Rep. 770. When a receiver should be appointed on a bill by stockholders of a corporation asking for such an appointment. Jones *v.* Pearl Mining Co., (Colo.) 38 Pac. Rep. 700; State *v.* Second Judicial District Court of Silver Bow County, (Mont.) 39 Pac. Rep. 316; Downing *v.* Coal Company, 93 Tenn. 221. When a stockholder is not entitled to have a receiver appointed for the corporation. Little Warrior Coal Co. *v.* Hooper, (Ala.) 17 So. Rep. 118. When a receiver should not be appointed. United Electric Securities Co. *v.* Louisiana Electric Light Co., 68 Fed. Rep. 673; Original

inspection of the books by this stockholder, and an affidavit filed with the bill charging that the president is insolvent, and since the inauguration of the suit had mortgaged all his real estate with intent to defeat the claim of the company, there being no allegation of fraud on the part of the other stockholders, but rather a distinct intimation that the president was sustained by them, and the solvency of the corporation being unquestioned, it has been held would not justify a court, before the time for answer has expired, in granting a motion for the appointment of a receiver, and thereby taking the corporation out of the control of the large majority of stockholders.[1] On a motion for a receiver of a corporation in this action, it was held that an allegation that the assets of the corporation were insufficient to pay all its liabilities, including its capital stock as a liability of the corporation to its stockholders, was not sufficient to show that the corporation was insolvent.[2] The United States Circuit Court for the western district of Virginia refused to appoint a receiver for a business corporation upon mere allegations of insolvency, unaccompanied by a charge of fraud, mismanagement or wasting of assets, whereby the plaintiff's claim would be imperiled. Besides, the plaintiff's affidavits as to insolvency were opposed by other affidavits denying the facts and alleging that the appointment of a receiver would be injurious to the interests of all parties, including creditors.[3] That the property of a corporation subject to levy under a judgment of a state court was unsalable by reason of its unmarketable condition, though valuable, and the further fact that the sheriff was so situated with reference to the property, that he could not execute the writ, has been held by the federal court

Vienna Bakery, Coffee & Natatorium Co. *v.* Heissler, 50 Ill. App. 406; Klee *v.* E. H. Steele Co., (Minn.) 62 N. W. Rep. 399; Doe *v.* North West Coal & Transportation Co., 64 Fed. Rep. 928; Cook *v.* East Trenton Pottery Co., (N. J. Eq.) 30 Atl. Rep. 534.

[1] Ranger *v.* Champion Cotton Press Co., (1892) 52 Fed. Rep. 609.

[2] Hagenbeck *v.* Hagenbeck Zoological Arena Co., (1893) 59 Fed. Rep. 14. When a corporation is insolvent. Corey *v.* Wadsworth, (Ala.) 11 So. Rep. 350, overruling Corrugating Co. *v.* Thacher, 87 Ala. 458; s. c., 6 So. Rep. 366; Woolverton *v.* George H. Taylor Co., 43 Ill. App. 424: Albitzue *v.* Guadelupey Caloo Min. Co., (Tenn.) 22 S. W. Rep. 739. As to when a corporation is insolvent, see Atwater *v.* American Exchange Nat. Bank, 152 Ill. 605; s. c., 38 N. E. Rep. 1017; Mish *v.* Main, (Md.) 31 Atl. Rep. 799; French *v.* Andrews, 81 Hun, 272; s. c., 30 N. Y. Supp. 796.

[3] Lawrence Iron Works Co. *v.* Rockbridge Company, (1891) 47 Fed. Rep. 755.

not sufficient to warrant the appointment of a receiver for the corporation by that court.[1] In this case it was held that the action of the directors, at a meeting of this corporation, the president, secretary and treasurer only were present, in voting themselves salaries, which, however, were never collected, was void, and certain irregularities in the management were not sufficient to justify appointing a receiver for the corporation, it being shown that no actual fraud was intended.[2] The Supreme Court of Wisconsin has declared these rules as to sequestration of the property of an insolvent corporation and having it administered through a receiver: "It is within the function of the Circuit Court to supervise and compel the directors of insolvent corporations to perform their duties as trustees for the corporate creditors in the administration of the corporate property. To that end, in a proper case, by sequestration, it will lay hold of the corporate estate and administer it by its receiver. A proper case for the intervention of the court arises whenever execution on a judgment against a domestic corporation has been returned unsatisfied. Then the court, in an action for that purpose by the execution plaintiff, will sequester the property and effects of the corporation and put it into the hands of a receiver to wind up its affairs and distribute its assets among its creditors.[3] To make the sequestration effectual, it will enjoin other creditors from pursuing their own remedies, and will compel all officers of the law to turn over to the receiver all property of the corporation held by them on attachment or execution, to the end that there shall be a fair and just division of the assets of the corporation among all its creditors, according to law."[4] A portion of the stockholders of a corporation have no absolute right to the appointment of a receiver, though the corporation be insolvent, in the absence of fraud or mismanagement.[5] The Supreme Court of Iowa has held that a court of equity has jurisdiction to appoint a receiver of a state banking association on the petition of a stockholder; and where it shows, and the facts are admitted, such a state of financial affairs of the bank as indicate its hopeless insolvency, a receiver

[1] Buckeye Engine Co. *v.* Donau Brewing Co., (1891) 47 Fed. Rep. 6 (creditor's bill).

[2] Hardee *v.* Sunset Oil Co., (1893) 56 Fed. Rep. 51.

[3] Rev. Stat. Wis. §§ 3216–3228.

[4] Ford *v.* Plankinton Bank, (Wis. 1894) 58 N. W. Rep. 766; citing in support of the rules Ballin *v.* Loeb, 78 Wis. 404; s. c., 47 N. W. Rep. 516.

[5] Denike *v.* New York & Rosendale Lime & Cement Co., 80 N. Y. 599.

should be appointed.[1] There was a receiver appointed in the United States Circuit Court for the northern district of Illinois for a building and loan association organized under the laws of that state. A receiver, afterwards appointed by a state court, applied to the United States court by petition, asking that the receiver appointed by the latter court be ordered to surrender to him the assets of the corporation. The petition was denied and the court upheld its jurisdiction in the matter, holding that courts of equity have jurisdiction to appoint receivers to administer the assets of insolvent corporations. Also that a shareholder in a building and loan association, the officers of which association had so mismanaged its affairs that its assets amounted to less than two-thirds of the capital paid in, was entitled to have the corporate assets placed in the hands of a receiver. Upon special points of objection to the jurisdiction of the United States court it was held that in such a suit by a shareholder for the appointment of a receiver of a corporation, the amount in controversy was the value of the entire corporate assets. The court also declined to dismiss the suit by the stockholder on the ground that the parties to the suit had been collusively arranged for the purpose of creating a case cognizable in the federal courts, as it appeared that the assets of the corporation were in different states, and that its shareholders resided in different states, and, therefore, it was desirable to have all the corporate affairs wound up under a homogeneous management.[2]

§ 526. **Removal of receivers and assignees.**— The United States Circuit Court for the district of Oregon ordered the removal of a receiver of a corporation who had been appointed at the suggestion of parties representing one of two hostile factions or interests in the corporation on the ground that he was the nominee of the hostile party bitterly opposed by the other, whose appointment was made in the mistaken belief that all interests were united in him.[3] In a Minnesota case, where a trusted

[1] Dickerson *v.* Cass County Bank, (Iowa, 1895) 64 N. W. Rep. 395.

[2] Towle *v.* American Building, Loan & Inv. Soc., (1894) 60 Fed. Rep. 131.

[3] Wood *v.* Oregon Development Co., (1893) 55 Fed. Rep. 901. The district judge said: "It was said by Mr. Justice MILLER, in Meier *v.* Railway Co., 5 Dill. 478: 'It becomes a duty of the court to see that its powers are exercised on principles of strict neutrality as regards the belligerents; and this can be done in this case by removing the representatives of these hostile interests and appointing a receiver, who, in feeling and in conduct, will be

and confidential employee of an insolvent corporation was selected for its assignee by its president, who held a majority of its stock, had obtained illegal preferences to indemnify him against his indorsements for the corporation, and who guaranteed the assignee a certain compensation for a specified time for his services as assignee, and such assignee, after accepting and entering upon the trust, made an agreement with said president and certain other preferred creditors who were not residents of this state, to hold and collect for them, as their trustee, securities in his hands as assignee which had been received by the insolvent as collateral to other securities delivered by it to such creditors as an illegal preference, retaining such collateral in its hands, and the assignee, to assist him in the performance of his trust as assignee, employed the former attorney of the insolvent, the Supreme Court held that the assignee should have been removed, under the circumstances stated, on the application of a minority in number or amount of the creditors.[1]

§ 527. **The rights of receivers and assignees as to property of insolvent corporations.**— A corporation in Wisconsin being insolvent, as charged, confessed judgment to certain creditors, and under their executions property of the corporation was sold by the sheriff; the moneys resulting therefrom being still in his hands, a receiver of the corporation having been appointed by a court having jurisdiction in the suit of other creditors, made his motion in the court for a sequestration of the moneys and an order that they be placed in his hands to be administered for the benefit of all the creditors of the corporation. There was an order for the money to be paid to the receiver, and from this the judgment creditor of the corporation appealed. Upon appeal the Supreme Court affirmed the order of the court below.[2] A cor-

strictly neutral and strictly honest.' The receiver is solely the officer of this court. He must be, in the full sense of the term, the 'representative of the court.' He is in no way the representative of either party. His past relations, the influences that secured his appointment, his sympathies, from whatever cause, must not be such as to predispose him either way. He must be the appointee of the court."

[1] In re Mast, Buford & Burwell Co., (Minn. 1894) 59 N. W. Rep. 1044.

[2] Ford *v.* Plankinton Bank, (Wis. 1894) 58 N. W. Rep. 766. NEWMAN, J., speaking for the court, stated in his opinion the law in that state in such cases to be as follows: "[The verified complaint of the receiver, taken to be true], charges, in effect, that the [corporation] is an insolvent corporation; that after it became in-

poration, before its insolvency, having pledged property with power of sale, a court, after appointing a receiver for such corporation, cannot compel the pledgee to turn over the property to its receiver without first requiring payment of the debt it was pledged to secure. Nor does the appointment of a receiver of the insolvent corporation in such case deprive the pledgee of the property of the right to sell the property in accordance with the

solvent, and while known to be insolvent, both by its directors and the appellant, it colluded and conspired with the appellant and certain others of its creditors named, for the purpose of securing to such creditors unjust and inequitable preference over other creditors of such insolvent corporation; that, as a means of effecting the object of such conspiracy, judgments were confessed by such insolvent in favor of such creditors, executions were issued upon such judgments, and property of the insolvent corporation, to a large amount, was sold, of which sales the moneys so in the hands of the sheriff, and directed to be turned over to the receiver, are the fruit." After stating these allegations the court said: "Assuming what is charged to be true, it seems quite clearly to show a proper case for the sequestration of the property and effects of the insolvent corporation, and *prima facie*, at least, that the appellant and the other creditors named are not justly entitled to the entire fund in the sheriff's hands to the exclusion of other creditors of the insolvent corporation." The court said, as to the contention of the appellant that the moneys in the sheriff's hands, made upon its executions, were not subject to sequestration as the property of the corporation, because it claimed the title to those moneys was in it (the appellant) and not in the corporation: "Probably the appointment of a receiver can affect only such property as is owned by the insolvent at the time of the appointment. And cases are cited which hold that moneys made on execution, while still in the hands of the sheriff, are the property of the creditor. This may be law, as between the debtor and his creditor, in an ordinary case; but it is not controlling here, because, for the purposes of this motion and appeal, it is assumed to be true that the moneys which are in the sheriff's hands are the fruit of an illegal combination between the directors of the insolvent corporation and the appellant for the purpose of giving to the appellant an illegal preference over its other creditors. This is a fraud upon the rights of the other creditors. Fraud taints whatever it touches. No right can grow out of a transaction which fraud has touched. So, upon the present showing, it is held that the moneys were properly directed to be turned over to the receiver as a part of the assets of the corporation. But this does not, of necessity, supersede or displace the appellant's right to the fund. If it has a valid lien, that lien will follow the fund into the hands of the receiver, and the fund will be administered accordingly. The order is not a final determination of its rights. The right is not to be determined on a mere motion; it is to be determined in the motion itself. The rights of the creditors are to be adjusted and determined by the final order or judgment in the action. The statute so directs. Section 3217 of the Revised Statutes provides that it shall be the duty of the court, in the final order in the motion, to direct a just and fair distribu-

contract of the pledger.[1] A court of equity will not take jurisdiction of a suit brought in aid of a judgment at law, where the bill avers that execution has been issued and levied upon the judgment debtor's property, and does not allege that such execution has been returned. In this case, it appearing that the insolvent corporation confessed judgment in a state court in favor of several creditors, and also made a voluntary assignment for the benefit of creditors, it was held that the federal court had no jurisdiction, at the suit of a creditor, brought after the sheriff and assignee had taken possession, to interfere with their disposition of the corporation's property.[2]

§ 528. Other rights of receivers and assignees of insolvent corporations.— Receivers of an insolvent corporation who by order of court collect accounts assigned by the corporation as security are entitled to compensation for their services out of the funds so collected.[3] A suit commenced before the appointment of a receiver of the property of a corporation, upon a claim afterwards filed, within the time limited, against the receiver, may be prosecuted to judgment, which, when rendered, establishes, as against the receiver, the amount of the claim. Should such a

tion of the property of such corporation and of the proceeds thereof among its fair and honest creditors in proportion to their debts, respectively, to be paid in the same order as prescribed in section 3245. Section 3245 provides that all lawful and equitable liens upon the property of such corporation shall be paid in the order of their priority, and before the common debts are paid. The remedy for the enforcement of such rights as the appellant may have is to be brought in the action where the whole estate of the insolvent corporation is being administered. That this is the regular and orderly proceeding in such cases is recognized and made clear by the decision in Aschermann *v.* Bank, (Wis.) 57 N. W. Rep. 349."

[1] National Exchange Bank *v.* Benbrook School Furnishing Co., (Tex. Civ. App. 1894) 27 S. W. Rep. 297; citing on first point Carter *v.* Hightower, 79 Tex. 135; s. c., 15 S. W. Rep. 223; In re Home Provident Safety Fund Assn., 129 N. Y. 288; s. c., 29 N. E. Rep. 323; Hudson *v.* Wilkinson, 61 Tex. 606; Goldfrank *v.* Young, 64 Tex. 437; Risk *v.* Banking Co., 58 Fed. Rep. 45; Schultz *v.* Jerrard, (N. J. Ch.) 3 Atl. Rep. 265; Beach Rec. §§ 80–82; Jones Pledges, §§ 720, 724, 739; King *v.* Insurance Co., 58 Tex. 669. As to power of receivers, see Showalter *v.* Improvement Co., 83 Tex. 162 As to duty of receivers, see Thompson *v.* Huron Lumber Co., 4 Wash. St. 600; s. c., 30 Pac. Rep. 741.

[2] Cleveland Rolling Mill Co. *v.* Joliet Enterprise Co., (1892) 53 Fed. Rep. 683.

[3] Preston Nat. Bank of Detroit *v.* Emerson, (Mich. 1894) 60 N. W. Rep. 981.

receiver know of the pendency of a suit on such a claim afterwards filed against him, a failure on the part of the claimant to refer to the pending suit at the time of the filing of the claim would not cause a waiver of the right to prosecute the action, or constitute an election of remedies. In such a case, however, the receiver should not be charged with the costs both of the suit and of the investigation of the claim before the master, and the creditor should only be allowed the amount of the judgment exclusive of the costs.[1] In a New Jersey case the assignee of one of the directors of an insolvent corporation filed a bill against the receiver of the corporation and others, for the administration of both estates and for the marshaling of assets, and the receiver of the corporation answered, and filed a cross-bill alleging that the directors of the corporation had declared and paid numerous dividends contrary to the statute, which limits their liability for the payment of such illegal dividends to the payment of six years prior to the commencement of the suit. Vice-Chancellor BIRD held in the action that it was competent for the receiver to show errors and falsifications of the accounts of the corporation at any reasonable time prior to the commencement of the period of six years within which suit to recover might be had. Also, that although the receiver represented the corporation and produced its books of account, this did not prevent him from contradicting the entries in the books, for the reason that he represented creditors also.[2] A manufacturing corporation had entered into a contract to deliver articles of its manufacture to one who was indebted to it upon its assignment for the benefit of creditors, it becoming insolvent. In an action by the assignee upon this open account the Supreme Court of Minnesota held that the defendant might set off his demand growing out of the contract to deliver goods and failure to deliver on the part of the corporation.[3]

[1] Pine Lake Iron Co. *v.* La Fayette Car Works (Adams, Intervener), (1893) 53 Fed. Rep. 853.

[2] Whittaker *v.* Amwell Nat. Bank (N. J. Eq. 1894) 29 Atl. Rep. 203.

[3] Laybourn *v.* Seymour, (1893) 53 Minn. 105; s. c., 54 N. W. Rep. 941. It was said by the court: "The unsigned order thus 'accepted' by the corporation constituted an express agreement on its part to deliver goods as therein specified; but that was the extent of its obligation in the first instance. While the conditions remained as they were when it was issued, the corporation could not be called upon to pay the specified amount in money nor could the 'acceptance' have been available as a set-off, under the statute against a

§ 529. **Insolvent beneficial associations — rules.**—A court of competent jurisdiction having, by the appointment of a receiver, assumed the administration of the funds of an insolvent benevolent association, it is competent for a court of equity in another state, on a bill filed for that purpose by the receiver, to pay over the funds in their hands to the receiver. And it is no objection to making such an order that the fund in question constitutes a reserve fund, which, by the rules of the association, the central authority could only call in at certain times and for certain purposes and not for the general purpose of liquidating the whole trust fund.[1] As to the distribution of the funds of a mutual benefit association, with branches in several states, becoming insolvent and placed in the hands of a receiver in Massachusetts, it was held that the benefit and reserve funds should be proportionally distributed among the certificate holders regardless of their residence. And to that end certificate holders who may have attached property of the association would be excluded from any share in such funds unless they released such attachments or accounted for the property in their possession.[2]

debt due to the corporation, of the nature of that for which this action is prosecuted; but the making of the assignment under the insolvent law changed the situation and the legal rights of the holder of this instrument. The corporation thereby disabled itself from performing the specific obligation expressed in its written undertaking, and hence subjected itself at once to the alternative liability to answer in damages as for breach of contract. The law does not require the doing of a useless thing, and the corporation having thus disabled itself to specifically perform its agreement, a demand was not necessary to convert the right to demand the goods into a right to compensation in money. The situation of defendants is the same as it would have been if, before the assignment in insolvency, they had demanded the goods, and the corporation, from inability to comply with the demand, or from other cause, had refused to deliver the same."

[1] Failey *v.* Talbee, (1893) 55 Fed. Rep. 892. It was said: "[The laws of the association] undoubtedly do impress upon the funds the character of trust funds, and, perhaps, affect different parts of the fund with different equities; but as to the time and manner of ascertaining and marshaling these equities, and as to the method of administration of the fund accordingly, they must be taken to be abrogated in the case where, as this bill alleges, the society is insolvent. The methods of the court are not to be substituted for the methods provided by the laws." As to the rights of receivers, one being appointed for the supreme body of a benevolent association, and one of a local branch of the same association, see Weiner *v.* Sturgiss, (Md. 1894) 29 Atl. Rep. 613.

[2] Garham *v.* Mutual Aid Society, (Mass. 1894) 37 N. E. Rep. 447. See Fogg *v.* Supreme Lodge, 156 Mass. 431; s. c., 31 N. E. Rep. 289.

§ 530. Liability of stockholders on unpaid subscriptions — the court's right to enforce and how enforced.— The Supreme Court of Tennessee has held that under a general assignment of its assets by an insolvent corporation for the benefit of its creditors, unpaid subscriptions, due from defendant shareholders, passed to the assignee, and that it was his duty to collect them and pay the proceeds to creditors, or, in case of a surplus, to the assignors. They also held that the assignee's right to recover such subscription was not defeated or lost, when, with his permission, the shareholders, other than such delinquent, reorganized the corporation and resumed business, issuing and selling preferred stock and borrowing money, thereby paying some of the debts and acquiring assets sufficient to meet others.[1] A judgment against a corporation and others jointly for the recovery of money is a debt of the corporation, for the purpose of enforcing, as against stockholders, liabilities for unpaid subscriptions and other statutory liability.[2] The doctrine has been declared by the United States Supreme Court that creditors of an incorporated company who have exhausted their remedy at law can, in order to obtain satisfaction of their judgment, proceed in equity against a stockholder to enforce his liability to the company for the amount remaining due upon his subscription to stock, although no account is taken of the other indebtedness of the company, and the other stockholders are not made parties; although, by the terms of their subscriptions, the stockholders were to pay for their shares "as called for" by the company, and the company had not in the case before the court called for more than thirty per cent of the subscriptions.[3] This was an action under the

[1] Cartwright *v.* Dickinson, (1890) 88 Tenn. 476; s. c., 12 S. W. Rep. 1030.

[2] Frost *v.* St. Paul Banking & Investment Co., (Minn. 1894) 59 N. W. Rep. 308.

[3] Hatch *v.* Dana, (1879) 101 U. S. 205. Mr. Justice STRONG, speaking for the court, said: "That unpaid subscriptions are to be regarded as a fund, which the corporation holds for the payment of its debts, is an undeniable proposition." He then states the contentions of the stockholders sued, to which the doctrine of the text is an adverse ruling, and said: "These positions, we think, are not supported by the authorities — certainly not by the more modern ones — nor are they in harmony with sound reason, when considered with reference to the facts of this case. The liability of a subscriber for the capital stock of a company is several, and not joint. By his subscription, each becomes a several debtor to the company, as much so as if he had given his promissory note for the amount of his subscription. At law, certainly, his subscription may be enforced against him without joinder of other subscribers, and in equity

General Statutes of 1878, chapter 76, of Minnesota, for the sequestration of the property of an insolvent corporation and to enforce the constitutional liability of its stockholders for the purpose of paying any balance of indebtedness existing after exhausting the corporate assets. The court held that the corpo-

his liability does not cease to be several. A creditor's bill merely subrogates the creditor to the place of the debtor, and guarantees the debt due to the indebted corporation. It does not change the character of the debt attached or garnished. It may be that, if the object of the bill is to wind up the affairs of this corporation, all the shareholders, at least so far as they can be ascertained, should be made parties, that complete justice may be done by equalizing the burdens, and in order to prevent a multiplicity of suits. But this is no such case. The most that can be said is that the presence of all the stockholders might be convenient, not that it is necessary. When the only object of a bill is to obtain payment of a judgment against a corporation out of its credits or intangible property, that is, out of its unpaid stock, there is not the same reason for requiring all the stockholders to be made defendants. In such a case, no stockholder can be compelled to pay more than he owes. In Ogilvie *v.* Knox Insurance Co., 22 How. 380, the question was considered. That was a case in which several judgment creditors of a corporation had brought a creditor's bill against it and thirty-six subscribers to its capital stock. The bill alleged that the complainants had recovered judgments against the company, upon which executions had been issued and returned 'no property;' that the other defendants had severally subscribed for its stock, and that the subscriptions remained unpaid, payment not having been enforced by the company. The prayer of the bill was that these other defendants might be decreed to pay their subscriptions, and that the judgments might be satisfied out of the sum paid. It was objected, as here, that the bill was defective for want of proper parties, but the court held the objection untenable. In delivering the opinion of the court, GRIER, J., said: 'The creditors of the corporation are seeking satisfaction out of the assets of the company to which the defendants are debtors. If the debts attached are sufficient to pay their demands, the creditors need look no further. They are not bound to settle up all the affairs of this corporation, and the equities between its various stockholders, corporators or debtors. If A. is bound to pay his debt to the corporation in order to satisfy its creditors, he cannot defend himself by pleading that these complainants might have got their satisfaction out of B. as well. It is true, if it be necessary to a complete satisfaction of the complainants that the corporation be treated as an insolvent, the court may appoint a receiver, with authority to collect and receive all the debts due to the company, and administer all its assets. In that way all the other stockholders or debtors may be made to contribute.' The court, therefore, directed a decree against the respondents severally for such amounts as appeared to be due and unpaid by each of them for their shares of the capital stock." The court cited, also, Bartlett *v.* Drew, 57 N. Y. 587; Pierce *v.* Milwaukee Construction Co., 33 Wis. 253; Marsh *v.* Burroughs, 1 Woods, 468; Wood *v.* Dummer, 3 Mason 308; and distinguished Pollard *v.* Bailey, 20

ration was not organized for the purpose of carrying on an exclusively manufacturing business, and its stockholders were liable for its debts to the amount of their stock. Also, that the court could not by construction limit this liability by holding that each stockholder was liable only ratably when some of the stockholders were insolvent or beyond the jurisdiction of the court; further, all those who were stockholders at the time the action was commenced were liable, although some of them were not stockholders at the time the corporate liability was incurred.[1] A corporation making an assignment for the benefit of creditors, under the laws of Minnesota relating to such assignments, the court has power to make calls for unpaid subscriptions to stock. And such a case, while it neither determines absolutely the liability of the stockholders, nor has the effect of a judgment, makes whatever the stockholders are liable for within the call become due and payable so that suit may be brought to enforce the liability.[2] The propriety of the call for unpaid subscriptions to stock in this case, and the justification of the call, was before the court. The contentions were such as to require the declaration of rules as to claims against such an insolvent corporation. The court held that under the law proof of claims against the insolvent corporation was, in the first instance, to be made to the receiver or assignee, and his decision upon them, if acquiesced in, would be final. But in case the receiver or assignee allowed a claim, any debtor or other party interested in the assets, or their distribution, might, before the decision of the receiver or assignee became final by acquiescence, apply to the court for, and would be entitled, upon the application, to have a judicial examination and decision as to the allowed claim. But such an examination should be

Wall. 520, and Terry *v.* Tubman, 92 U. S. 156.

[1] First Nat. Bank of Winona *v.* Winona Plow Co., (Minn. 1894) 59 N. W. Rep. 997; citing on the last point, Gebhard *v.* Eastman, 7 Minn. 56.

[2] In re Minnehaha Driving Park Assn., (1893) 53 Minn. 423; s. c., 55 N. W. Rep. 598. The court said: "What remains unpaid on the subscriptions are debts due the corporation, and are its assets. When it is insolvent, they constitute a fund for the payment of its debts. It is true that, as the primary purpose of the proceedings in insolvency is to apply the assets to payment of the debts, the power of the court to make or direct calls for the unpaid subscriptions, and direct the enforcement thereof, must be limited to cases where it is necessary to resort to that fund for the purpose, and the extent of the call must be determined by the amounts of the debts and of the other assets."

applied for in a direct proceeding, and not be a part of, or collateral to, some other proceeding, such as a proceeding to authorize a dividend or to call in the assets.[1] This action by an assignee of an insolvent corporation was brought to recover from its stockholders unpaid stock subscriptions. The complaint alleged merely that no part of the stock owned and held by the several defendants had been paid, except a certain specified amount. The Supreme Court held that evidence was inadmissible to prove that the corporation had accepted, in payment of the stock, property that was greatly undervalued and grossly inadequate in value to the par value of the shares.[2] They held also that it was not an abuse of discretion in the court below to refuse to allow the complaint to be amended on the trial.[3] The Minnesota Supreme Court has held that the statutory liability of stockholders for corporate debts cannot be enforced in insolvency proceedings against the corporation under the act of 1881, but, pending such insolvency proceedings, the creditors may bring an action to enforce the liability of stockholders in an insolvent corporation under the General Statutes of 1878, chapter 76, section 17, in which the court may at once determine the maximum liability of each stockholder, and await the result of the insolvency proceedings to ascertain how much of it shall be enforced by execution.[4]

[1] In re Minnehaha Driving Park Assn., (1893) 53 Minn. 423; s. c., 55 N. W. Rep. 598.

[2] Smith *v.* Prior, (Minn. 1894) 59 N. W. Rep. 1016. The court said: "The cause of action thus attempted to be proved was not one in favor of the corporation, and founded on contract, but one in favor of creditors, and founded on fraud. Hospes *v.* Car Co., 48 Minn. 174; s. c., 50 N. W. Rep. 1117."

[3] Smith *v.* Prior, (Minn. 1894) 59 N. W. Rep. 1016.

[4] Olson *v.* State Bank, (Minn. 1894) 59 N. W. Rep. 635. It was said by the court: "The question was indirectly before us in State *v.* Bank of New England, 56 N. W. Rep. 575, in which it was stated, as a distinction between proceedings against an insolvent corporation under General Statutes of 1878, chapter 76, and insolvency proceedings under the act of 1881, that, under the former proceedings, directors and stockholders may be brought in, and their liabilities to creditors enforced; and it was assumed, or taken for granted, that this cannot be done under the latter proceedings. Chapter 76 clearly contemplates bringing in stockholders for that purpose. If this were not so, then, so far as that chapter is concerned, the creditors would be left to a suit in equity to enforce any liability of stockholders other than such as are deemed assets of the corporation. The statute determines the scope and compass of every special proceeding provided by it, and if authority is not found, either in express terms or by implication, in a statute regulating a special proceeding, for doing a particular thing, there

There has been much litigation growing out of a decree of the Chancery Court of Richmond, Virginia, in the case of what was, at first, a bill of a creditor who had obtained a judgment in Maryland against a Virginia corporation which had become insolvent, and finally its whole business had been abandoned, with a large amount of indebtedness, and no effort on its part to call for and collect out of its unpaid subscriptions to stock, which was eighty per cent of its capital stock, to pay its indebtedness. This creditor's suit was brought against the insolvent corporation, proper service being secured upon it and the trustees named in a certain trust deed executed by the corporation to them for the benefit of its creditors of all its estate, including money payable on assessments, requiring payment of all its debts, but reserving enjoyment for a specified period. Charges of inefficiency and disposition not to enforce the trust were made against these trustees and their removal asked. They were removed in the suit and a trustee substituted, and in his name the proceedings continued, finally resulting in a decree that he recover, by suit or otherwise, of the stockholders an assessment ordered by the court of thirty per cent of their unpaid subscriptions to be applied to the payment of the corporation's large indebtedness. There was no appeal from this decree. In one of the actions brought by this trustee to recover the assessment ordered against the estate of one of the subscribers to stock in Virginia, the case reached the Court of Appeals of that state. This court made these rulings upon the trust deed and the decree of the Chancery Court: The trust deed, construed, as it must be, by the laws of Virginia, was valid; it passed title to all unpaid subscriptions, with power to collect same to extent

is no authority. In Spilman *v.* Mendenhall, (Minn.) 57 N. W. Rep. 468, it was held that the proceeding regulated by General Statutes of 1878, chapter 34, sections 415 to 420, inclusive, being one to dissolve a corporation, settle its business, and convert its assets and apply the proceeds to payment of its debts, stockholders cannot be brought in to answer to their statutory liability, for the reason that the statute does not so provide, though they may be to enforce unpaid subscriptions, because such are assets of the corporation. And it is the same with insolvency proceedings under the law of 1881. There is nothing in that law to suggest that any remedy of creditors who come into the proceeding can be enforced, except as to the assets of the debtor. It is a proceeding merely to convert such assets and apply the proceeds upon the claims of such creditors as come in, and comply with the terms of the law." Actions of receivers of insolvent corporations against stockholders for unpaid subscriptions to stock. Elderkin *v.* Peterson, 8 Wash. 674; s. c., 36 Pac. Rep. 1089.

of call; that the decree of the Chancery Court bound not only the company but the stockholders also, whom the plaintiff, as such trustee and assignee, might, under, and also independently of, the Code of Virginia, sue in his own name for the amount of the call on their subscriptions.[1] Where a court of equity, at a suit of a creditor of an insolvent corporation, directs an assessment on the unpaid stock, such assessment, even though by reason of collusion in obtaining the decree it be larger than necessary to pay the debts, is no invasion of the stockholder's absolute rights, his obligation being that of a debtor to the corporation in the full amount of his subscription. And in such a case a different court would not entertain a suit to enjoin the collection of the assessments directed, so long as it was within the power of the court directing it to correct its mistake by reducing the assessment, or by ordering a ratable return of any surplus remaining after payment of the debts.[2] In one of the suits brought by this

[1] Lewis' Admr. *v.* Glenn, Trustee, (1888) 84 Va. 947. As to the validity of the trust deed, the court cited B. & O. R. R. Co. *v.* Glenn, 28 Md. 287. As to the service upon the company, etc., Glenn, Trustee, *v.* Williams, 60 Md. 93, and authorities there cited.

[2] Furnald *v.* Glenn, (1893) 56 Fed. Rep. 372. TOWNSEND, D. J., said: "In Graham *v.* Railroad Co., 118 U. S. 161; s. c., 6 Sup. Ct. Rep. 1009, the Supreme Court approved the statement of law made by Judge NELSON in the Circuit Court (14 Fed. Rep. 753) as follows: 'In Nougue *v.* Clapp, 101 U. S. 551, it was held that the Circuit Court of the United States cannot revise or set aside a final decree rendered by a state court which had complete jurisdiction of the parties and subject-matter upon the ground that the decree was obtained by fraud, where the injured party has had an opportunity to apply to the state court to reverse the decree. The plaintiff is a party to the foreclosure suit as a shareholder in the old corporation. The state court is still open to listen to the complaint of the corporation and its shareholders. The decree of the foreclosure, though final in one sense, as determining the respective rights of the parties to the property in question, is still in its nature interlocutory, and is open to review by the court, upon petition or motion in the cause, or by bill of review, for good cause shown. The plaintiff has, therefore, an ample and complete remedy for all his alleged grievances in the state court, and there is no occasion for his application to this court for relief by bill in equity.' Judge NELSON in that part of his opinion immediately preceding the foregoing quotation, laid down the rule upon which the complaint relies, with its limitations, as follows: 'It is well settled in the courts of the United States that when a decree or judgment has been obtained against a party to a suit at law or in equity by fraud or deception practiced upon him by his opponent, and he has lost, without fault of his, his remedy of applying to the court for the revocation or reversal of the decree or judgment, a court of equity will afford him relief.' Foster *v.* Railroad Co., 146 U. S. 88; s. c., 13

trustee against a subscriber to shares living in West Virginia to recover the assessment decreed against him, the United States Circuit Court of Appeals for the fourth circuit has held, lately, that in such an action it was no defense that the liability of certain other stockholders on their subscriptions had previously been compromised by the creditors for less than the amounts due, when it appeared that the entire unpaid subscriptions of all the stockholders had to be exhausted in order to satisfy the creditors' claims.[1] The trustee named in a trust deed of the property of a corporation to secure bonds had, for default in interest, demanded possession and it was surrendered to him. Afterwards the trustee filed a bill for foreclosure, and to have a receiver appointed, and to secure unpaid subscriptions of stock from stockholders and an application of the assets for the benefit of the creditors of the corporation. Unsecured creditors having obtained judgment against the corporation, subsequent to the execution of this mortgage, filed a bill alleging the invalidity of the trust deed above referred to, and also praying that the assets of the corporation, unpaid subscriptions, etc., should be, as a result of their proceeding, applied to the payment of their claims. In the meantime, there had been, in the foreclosure suit, a decree of foreclosure and sale of the property. In the United States Circuit Court this later bill was dismissed on its merits. The United States Supreme Court, on appeal, approved the dismissal of the bill but upon the ground of jurisdiction. In discussing this point of the case, it was said by Mr. Justice Brewer, speaking for the majority of the court (Justices Brown and Jackson dissenting):

Sup. Ct. Rep. 28; Kent *v.* Iron Co., 144 U. S. 75; s. c., 12 Sup. Ct. Rep. 650. See Glenn *v.* Marbury, 145 U. S. 499; s. c., 12 Sup. Ct. Rep. 914; Foote *v.* Glenn, 52 Fed. Rep. 529."

[1] Bennett *v.* Glenn, Trustee, (1893) 55 Fed. Rep. 956. Fuller, Circuit Justice, said: "It is well settled that decrees against a corporation of the character of those referred to in the pleadings necessarily bind the stockholders in the absence of fraud, and cannot be reviewed or impeached in collateral suits on assessments thereby made. Hawkins *v.* Glenn, 131 U. S. 319; s. c., 9 Sup. Ct. Rep. 739; Glenn *v.* Liggett, 135 U. S. 533; s. c., 10 Sup. Ct. Rep. 867. The decrees [in the Chancery Court of Richmond, Virginia] determined that the entire unpaid balance of the stock subscription was necessary in order to pay the indebtedness of the corporation. The judgment recovered against Bennett in 1884, and paid by him, determined his liability as a holder of fifty shares of stock, and defendants were to that extent at least, concluded in this second suit. Nesbit *v.* Independent Dist., 144 U. S. 610; s. c., 12 Sup. Ct. Rep. 746."

"The plaintiffs were simple contract creditors of the company, their claims had not been reduced to judgment, and they had no express lien by mortgage, trust deed or otherwise. It is the settled law of this court that such creditors cannot come into a court of equity to obtain the seizure of the property of their debtor, and its application to the satisfaction of their claims, and this, notwithstanding a statute of the state may authorize such a proceeding in the courts of the state. The line of demarcation between equitable and legal remedies in the federal courts cannot be obliterated by state legislation. Scott *v.* Neely, 140 U. S. 106; Cates *v.* Allen, 149 U. S. 451. Nor is it otherwise in case the debtor is a corporation and an unpaid stock subscription is sought to be reached. National Tube Works Company *v.* Ballou, 146 U. S. 517; Swan Land & Cattle Company *v.* Frank, 148 U. S. 603, 612. Nor is this rule changed by the fact that the suit is brought in a court in which, at the time, is pending another suit for the foreclosure of a mortgage or trust deed upon the property of the debtor." [1]

[1] Hollins *v.* Brierfield Coal & Iron Co., (1893) 150 U. S. 371, 378, 379. The court further said: "Doubtless in such foreclosure suit the simple contract creditor can intervene, and if he has any equities in respect to the property, whether prior or subsequent to those of the plaintiff, can secure their determination and protection; and here, by the express language of the bill filed by the trustee, all claimants and creditors were united to present their claims and have them adjudicated. These plaintiffs did not intervene, though, as shown by the allegations of their bill, they knew of the existence of the foreclosure suit; neither did they apply for a consolidation of the two suits. On the contrary, the whole drift and scope of their suit was adverse to that brought by the trustee, and in antagonism to the rights claimed by him. They obviously intended to keep away from that suit, and maintain, if possible, an independent proceeding to have the property of the debtor applied to the satisfaction of their claims. But this, as has been decided in the cases cited, cannot be done. The excuse suggested, that the rule which forbids in a suit to foreclose a mortgage the litigation of a title adverse to that of the mortgagor prevented them from intervening, is not sound. Their rights, like those of the trustee and the bondholders, were derived from the corporation defendant. Each claimed under it, and the validity and amount of such claims were matters properly and ordinarily considered and determined in a foreclosure suit. It is true the corporation might admit the validity of any or all of the claims, and then the validity could only be a subject of inquiry as between the claimants for the purpose of determining the matter of priority, but to that extent, at least, both validity and amount are always open to contest and determination." As to enforcing the liability of a corporation holding unpaid shares of the stock of an insolvent corporation, though it may have taken the shares

§ 531. **Creditor's bills — equitable jurisdiction.**— KEY, D. J., in the United States Circuit Court for the eastern district of Tennessee, sustained the court's jurisdiction in a creditor's bill brought against a railroad construction company, praying an injunction and the appointment of a receiver, upon allegations that the same persons engaged in building a railroad organized the construction company; that nearly all the bonds of the railroad company were issued to it; that the railroad company was insolvent, and in the hands of a receiver, and a decree of foreclosure had been rendered; that the promoters of both companies acquired control of large quantities of the bonds, and in equity held them as trustees for the construction company; that they conspired to strip this latter company of its assets, and in pursuance of the conspiracy diverted large sums of money from its treasury, and pledged its bonds for debts for which it was not liable, and that the construction company was insolvent. The court held that, as it appeared that one of the complainants had a judgment obtained in another state, the bill, as far as he was concerned, might be maintained in the federal court, though his judgment was procured in another state than that in which the federal court sat.[1] Also that the allegations of the bill were sufficient to sustain equity jurisdiction, although the other creditors had not procured judgments as the basis of the suit.[2] The creditors of an insolvent mercantile corpora-

as collateral security for a debt, see Calumet Paper Co. *v.* Stotts Investment Co., (Iowa) 64 N. W. Rep. 782. As to the liability of a stockholder of a bank for the debts of the bank under Minnesota statutes, see Harper *v.* Carroll, (Minn. 1895) 64 N. W. Rep. 145. Rules as to courts' rights to call for unpaid subscriptions to stock of insolvent corporations and the right of receivers and assignees to enforce the liability. Barcalow *v.* Totten, (N. J. Eq.) 32 Atl. Rep. 2; Bennett *v.* Great Western Telegraph Co., 53 Ill. App. 276; Great Western Telegraph Co. *v.* Loewenthal, 154 Ill. 261; s. c., 40 N. E. Rep. 318, affirming 51 Ill. App. 447; Furnald *v.* Glenn, 12 C. C. A. 27; s. c., 64 Fed. Rep. 49.

[1] Merchants' Nat. Bank *v.* Chattanooga Construction Co., (1892) 53 Fed. Rep. 314, following Stutz *v.* Handley, 41 Fed. Rep. 527; Handley *v.* Stutz, 139 U. S. 417: s. c., 11 Sup. Ct. Rep. 530.

[2] Merchants' Nat. Bank *v.* Chattanooga Construction Co., (1892) 53 Fed. Rep. 314. It was said: "Bills in equity, with far fewer elements of original jurisdiction, have been maintained. In the case of Stutz *v.* Handley, 41 Fed. Rep. 537, * * * the court says of that suit: 'Its object being to reach and subject a trust fund, complainants were not even required to have reduced their claims to judgment, and exhausted the remedy at law, after the involving of the company.' Citing Case *v.* Beauregard, 101 U. S. 688–690. Judge HARLAN says in Mellen *v.* Iron Works, 131 U. S. 367; s. c., 9 Sup. Ct. Rep. 781: 'The

tion, the corporators of which, having the full and absolute control of its affairs, having wrongfully misappropriated its assets, so as to put the same beyond the reach of these creditors, may, though the claim of each be separate and distinct from those of all the others, unite in an equitable petition for the purpose of subjecting these corporators to individual liability, because of such misappropriation; and to the end of obtaining an accounting by them for the assets thus misappropriated, the corporation itself is a proper party co-defendant in such petition.[1] The United States Circuit Court of Appeals for the fifth circuit reversed a decree granting an injunction in the United States Circuit Court for the southern district of Georgia, and ordered the injunction dissolved upon a bill in equity seeking to subject the property of a railroad company to the payment of the simple contract debts of the complainants. In their bill they charged that the defendant railroad company was insolvent, and was about to put out an issue of second mortgage bonds for purposes and on a scheme that would work an injury to them as unsecured creditors, and asked for the appointment of a receiver and for an injunction. The Court of Appeals held that the Circuit Court had no jurisdiction of a bill in equity to subject the property of an insolvent corporation to the payment of a simple contract debt in advance of a recovery of a judgment at law, when such debt was unsecured by lien or mortgage, notwithstanding the statute of the state authorized the bringing of such suit by any three creditors of the insolvent corporation.[2]

removal of alleged liens or incumbrances upon property, the closing up of affairs of insolvent corporations, and the administration and distribution of trust funds are subjects over which courts of equity have general jurisdiction.' When insolvency proceedings may be instituted against an insolvent corporation, Marble *v.* Jamesville Mfg. Co.. (Mass.) 39 N. E. Rep. 998; Steel Edge Stamping & Retinning Co. *v.* Manchester Savings Bank, (Mass.) 39 N. E. Rep. 1021. Rules governing creditors' actions to enforce their rights against assets, etc., of insolvent corporations, see J. W. Butler Paper Co. *v.* Robbins, 151 Ill. 588; s. c., 38 N. E. Rep. 153; Moulton *v.* Connell-Hall-McLester Co., 93 Tenn. 377; s. c., 27 S. W. Rep. 672.

[1] Pullman *v.* Ellis, (Ga. 1895) 22 S. E. Rep. 568. As to the rights of a creditor whose execution against a corporation has been returned *nulla bona* to proceed by bill for a sequestration of the effects of a corporation, see Judson *v.* Rossie Galena Co., 9 Paige, 598. As to the proper mode in New York to obtain a sequestration of a corporation's assets, see Corning *v.* Mohawk Valley Insurance Co., 11 How. Pr. 190.

[2] Atlanta & Florida R. Co. *v.* Western Ry. Co. of Alabama, (1892) 50 Fed. Rep. 790. McCormick, Circuit Judge, said: "The bill in [Terry *v.* Anderson,

§ 532. Claims against insolvent corporation — rules as to allowances, etc.— Upon the petition of certain banks which had made loans to a savings bank in Nebraska and held collaterals for their loans in insolvency proceedings against such savings bank, the questions to be decided were thus stated by the Nebraska Supreme Court: "Are these plaintiffs, the banks, entitled to have their claims against the general assets of the savings bank? And

95 U. S. 628, cited by appellee] was against the trustees and stockholders to enforce against the stockholders of the insolvent bank the liability of said stockholders for the unredeemed bills of the bank, some of which bills complainants held. Demurrers, not distinctly raising the question we are considering, were sustained, and the bill dismissed, and, in delivering the opinion of the court affirming the decree of the Circuit Court, Chief Justice WAITE says: 'The complainants are, neither of them, judgment creditors of the bank. In a suit instituted by the assignees to close up the assignment, they proved their claims, and the amount due them was found for the purposes of a division. The finding was sufficient for the purposes of distribution, but it has none of the characteristics of a judgment or decree, to be enforced as against anything but the fund which the court was then administering.' At a subsequent day of the term, in overruling a petition for rehearing, he used this language quoted in the brief of appellee's counsel: 'Ordinarily a creditor must put his demand into judgment against his debtor and exhaust his remedies at law, before he can proceed in equity to subject choses in action to its payment. To this rule there are, however, some exceptions, and we are not prepared to say that a creditor of a dissolved corporation may not, under certain circumstances, claim to be exempted from its operation. If he can, however, it is upon the ground that the assets of the corporation constitute a trust fund which will be administered by a court of equity, the principle being that equity will not permit a trust to fail for want of a trustee.' The case of Graham *v.* Railroad Co., 102 U. S. 148, cited by appellees, was a bill by judgment creditors of the railroad to subject certain lands alleged to have been fraudulently obtained from the railroad, to the payment of complainant's judgments. The bill was dismissed on demurrer. The question we are now considering was not in the case, and the concluding paragraph of Judge BRADLEY'S opinion, quoted by appellees' counsel, does not touch the question as to the appellees here being proper parties to bring the bill they have exhibited against appellants. Appellees' counsel quotes the second paragraph of the syllabus in the report of the case of Mellen *v.* Iron Works, 131 U. S. 353; s. c., 9 Sup. Ct. Rep. 781, which appears to sustain the contention of appellees. In the body of the opinion we note this language: 'It is, however, contended that the furnace company could not rightfully invoke the aid of a court of equity to remove this lien or incumbrance until it had, by obtaining judgment for its debt, and suing out execution, exhausted its legal remedies. Jones *v.* Green, 1 Wall. 330; Van Weel *v.* Winston, 115 U. S. 228, 245; s. c., 6 Sup. Ct. Rep. 22. But that was one of the questions necessary to be determined in the suit brought by that company, and any

if so, in what amount? For the whole original sum of the loans and interest, or must they deduct any and all sums collected of the collaterals, and prove their claim for the balance? And should a similar deduction be made before each dividend declared by the receiver? Each bank to receive, at each time the dividend is declared, only such amount as the balance remaining due it after such deduction entitles it? And if they are entitled to share in the general assets, should they be required, as a condition precedent thereto, to deliver the collaterals held by them to the receiver, to be by him collected or disposed of should the court so order, for the benefit of these banks, and applied on their claim until it is extinguished, or fully paid?" The court fully discussed the different rules which had been declared in different jurisdictions and adopted as in their judgment the proper one that all sums collected from the collaterals be deducted, and proof made for the balance of the claim, and, immediately before, or at the time of each dividend, all sums derived from the collaterals between the date of proof and the date of such dividend be deducted from the claim, and the creditor draw dividends according to the balance.[1] One holding claims against an insolvent corporation in the process of being wound up, partly secured by first

error in deciding it would not authorize even the same court in an original independent suit, to treat the decree as void. * * * In the view we take of the case, it is not necessary to determine the soundness of any of these propositions, for if the court erroneously ruled upon any of them, its decree could not, for that reason, be asserted in a collateral proceeding as void for want of jurisdiction.' And we take it that the Supreme Court, in this case, expressly did not decide the question we are now considering."

[1] State ex rel. Attorney-General v. Nebraska Savings Bank, (Neb. 1894) 58 N. W. Rep. 976. The court said: "We are satisfied that [the rule] is the true one, and that it will, in its present workings, result in keeping the parties in as near the exact relations they occupied, as to enforcement of their claims, before the appointment of the receiver, and in greater equity, fairness, equality, and justice than can be attained in any other manner, and hence we conclude to adopt it." As to the collaterals, it was then said: "What should be done with the collaterals has been variously determined by the courts which agreed on the main rule as to proof of the claim or claims, but we think the best and most equitable disposition that can be made of them is that they be delivered to the receiver, to be by him held and collected, or otherwise disposed of if the court so orders, and the amount realized in either manner, or both, if favored, to be applied by him to the payment of the debt due the banks until these sums, together with the dividend, result in cancelling the indebtedness, or both funds are exhausted; the remainder, if any, then to be and become a part of the general assets, and for the benefit of all

mortgage on the property, and receiving an amount from the sale of the property of the corporation sufficient to pay the part secured by mortgage, the Illinois Supreme Court has held, was not entitled to be paid in the distribution dividends proportioned to the entire amount of his claims. The dividend should have been upon the residue of his claim.[1] It appearing that the notes of the corporation, which in this case was in the hands of a receiver as insolvent, were given payable at twelve months out of the first net earnings for a loan made to the corporation by its stockholders under an agreement between themselves to meet a certain indebtedness of the corporation, the corporation's liability on the notes was held to be limited to the net earnings, and, there being no net earnings applicable to the payment of the notes, there could be no recovery upon them either by the stockholders or those to whom they assigned them.[2]

§ 533. **Rules in cases of insolvent banks.**— Depositors in a bank which may be a state depository may set off their deposits against notes of theirs due the bank in the hands of a receiver of the bank. The lien of the state for the bank's indebtedness to it affects only the balances due on such notes after the set-off of the deposits due the makers.[3] A check on a suspended bank acquired

creditors; the expense of the collection of collaterals to be paid from such collections, and the general assets not to be chargeable with such expense; and no expense of collecting other assets to be paid from moneys derived from the collaterals; the receiver to be paid such compensation for holding the collaterals as shall be ordered by the court to be paid from the proceeds of the collaterals. By this we think the collaterals will be more rapidly made, and at less expense; and any favorable controversy between the receiver and the creditors holding the securities, in reference to it, or failure to collect or enforce it on their part, will be avoided." That a creditor cannot prove both his original claim and collateral obligations of the corporation creating a lien upon its property, see People v. Remington, 121 N. Y. 675, affg. 54 Hun, 480.

[1] First Nat. Bank of Peoria *v.* Commercial Nat. Bank of Peoria, (Ill. 1894) 37 N. E. Rep. 1019. The court distinguished, Re Bates, 118 Ill. 524; s. c., 9 N. E. Rep. 257. In Watson *v.* New Jersey Chemical Co., (N. J. Eq. 1894) 29 Atl. Rep. 186, Vice-Chancellor GREEN, a firm having transferred to a creditor, a claim against the corporation which subsequently had become insolvent, held that the dividend declared by the receiver should be applied on such indebtedness instead of on notes upon which the firm was accommodation indorser for the corporation.

[2] Lyman *v.* Northern Pac. Elevator Co., (1894) 62 Fed. Rep. 891.

[3] State *v.* Brobston, 94 Ga. 95; s. c., 21 S. E. Rep. 146. See Davis *v.* Manufacturing Co., 114 N. C. 321.

with a knowledge of its suspension by a debtor to that bank cannot be set off by him against his debt to the bank, though the check may have been acquired before a receiver for the bank was appointed.[1] A trust in favor of a principal will not be impressed upon the assets of an insolvent bank, giving him a preference over its other creditors by the simple fact that his agent deposited money in another than his own name with notice to the bank that it was the money of third parties.[2] Where a special depositor with a bank on being falsely told that there were not sufficient funds in bank to pay the amount held in trust by the bank for him, received in part payment a draft which was never paid, the Supreme Court of Michigan held that there was in the circumstances no waiver of his right to impress upon the assets of the insolvent bank a trust in his favor.[3] That a bank receiving money as agent for another, mingled it with its own funds, has been held in Michigan not to prevent the imposition of a trust for the amount on the insolvency of the bank, where the money in hand in the bank at the time prior to its failure was reduced below the amount in this manner received in trust by it.[4] A check given to the bondsman of a city treasurer by an insolvent bank for the amount of the first dividend on the claim of the city for a deposit of city funds by its treasurer was turned over to the city treasurer and credited on his account with the city. The Kansas Supreme Court has held that the amount of such check was a trust fund which might be recovered by the city from the assignee of the bank.[5] Where a holder of a bank certificate of deposit had become suspicious of the bank's solvency and withdrew a part of his deposit and took a certificate for the balance, upon an agreement that this balance should be put in a separate package, subject to his order, but it was not done, the Illinois Appellate Court held that this balance of money to his credit was not sufficiently distinct from the other funds of the bank to impress a trust in favor of the depositor on the insolvency of the bank.[6] The Supreme Court of Georgia has in a

[1] Avery *v.* Ladd, (Or.) 38 Pac. Rep. 1088.

[2] Henry *v.* Martin, 88 Wis. 367; s. c., 60 N. W. Rep. 263.

[3] In re Johnson, (Mich.) 61 N. W. Rep. 352.

[4] Ibid.

[5] City of Larned *v.* Jordan, (Kans.) 39 Pac. Rep. 1030.

[6] Bayor *v.* Schaffner & Co.'s Estate, 51 Ill. App. 180.

late case held that where a bank, having money on deposit with another, failed in business and became insolvent, being at the time indebted to the depositary upon promissory notes the sum total of which exceeded the amount of the deposit, it was the right of the depositary by way of equitable set-off to appropriate the money on deposit, as far as it would go, to the satisfaction of such notes, although they had not yet become due. In such case ordinary checks payable to the order of named persons drawn upon the depositary by the first bank before its failure, but not made payable specifically out of the fund on deposit, were neither assignments nor appropriations *pro tanto* of that fund, so as to bind the drawee to pay the same notwithstanding the drawer's failure. It was the right of the depositary after crediting the deposit upon the notes it held against the failing bank, to share upon the balance still due *pro rata* with the depositors of that bank in a general distribution of its assets in the hands of a receiver who had been appointed to take charge of and administer the same.[1]

[1] Georgia Seed Co. *v.* Talmadge, (Ga. 1895) 22 S. E. Rep. 1001. As to the point with reference to the checks upon the depositary not operating as an assignment, the court cited Baer *v.* English, 84 Ga. 403; s. c., 11 S. E. Rep. 453; Haas *v.* Bank, 91 Ga. 307; s. c., 18 S. E. Rep. 188; Jones *v.* Glover, 93 Ga. 484; s. c., 21 S. E. Rep. 50. As to the right of equitable set-off, see Kentucky Flour Co.'s Assignee *v.* Merchants' Nat. Bank, (Ky.) 13 S. W. Rep. 910; Nashville Trust Co. *v.* Fourth National Bank, (Tenn.) 18 S. W. Rep. 822; Jones *v.* Robinson, 26 Barb. 310. For a case holding that a county treasurer was not entitled to a preference over other creditors to certain moneys among the assets of an insolvent banker making an assignment for the benefit of his creditors, see Stevens *v.* Williams, (Wis. 1895) 64 N. W. Rep. 422. As to the right to recover from receivers of insolvent banks moneys received on deposit by banks with a knowledge of their insolvency, see Lake Erie & Western R. R. Co. *v.* Indianapolis Nat. Bank, 65 Fed. Rep. 690; Grant *v.* Walsh, 145 N. Y. 502; s. c., 40 N. E. Rep. 209; American Trust & Savings Bank *v.* Gueder & Paeschke Manufacturing Co., 150 Ill. 336; s. c., 37 N. E. Rep. 227, affirming 51 Ill. App. 349. As to rules governing in cases of criminal prosecution of officers of banks under statutes in various states for receiving deposits knowing the banks to be insolvent, see State *v.* Myers, 54 Kans. 206; s. c., 38 Pac. Rep. 296; Commonwealth *v.* Sponsler, 16 Pa. Co. Ct. Rep. 116; Carr *v.* State, (Ala.) 16 So. Rep. 150; Koetting *v.* State, 88 Wis. 502; s. c., 60 N. W. Rep. 822; State *v.* Buck, 120 Mo. 479. That the statute of Iowa as to criminal acts of officers of banks applies to officers of national banks, see State *v.* Fields, (Iowa) 62 N. W. Rep. 653.

As to "Insolvency of Private Corporations," see further, chapter XIII, "Insolvency of Banks," and chapter XIV, "Liability of Shareholders."

CHAPTER XXVIII.

FORECLOSURE OF MORTGAGES AND TRUST DEEDS.

§ 534. Jurisdiction of actions to foreclose.
535. Bringing such actions — rules.
536. Parties to such actions.
537. General rules as to such actions.
538. Decrees in such actions — general rules.
539. Decrees for sale of property.
§ 540. Purchasers at sales under the decrees — their rights and liabilities.
541. Who may be heard on petition in foreclosure suits.
542. Disposition in decree of proceeds of sale.
543. Allowances in forclosure suits

§ 534. **Jurisdiction of actions to foreclose.**— A federal court, having jurisdiction and possession, through its receiver, of all the property of a railroad company, thereby acquires jurisdiction of a subsequent suit to foreclose a mortgage on the same property, irrespective of the citizenship of the parties thereto, and may enter in such suit a binding decree of foreclosure and sale.[1] There is no jurisdiction or power in a state court to interfere with a decree of foreclosure made in a federal court against a railroad company where the railroad was within the jurisdiction of the court making the decree, and all the parties in interest were before it.[2] It has been held in the United States Circuit Court for the eastern district of Tennessee that the provision in the federal statute of August 13, 1888, that in any suit to enforce any legal or equitable lien on, or claim to, or to remove any lien or cloud upon, property situated in the district where the suit is brought, defendants who are not inhabitants thereof may be made parties, and brought into court by the methods there prescribed, applied to an original bill, brought for the purpose of enforcing various liens upon part of a railroad lying in the district, as against the lien of a general mortgage, which is about to be foreclosed in the same court by a suit ancillary to another suit in a different district and state. The court, therefore, held the original bill filed

[1] Carey *v.* Houston & Texas Cent. Ry. Co., (1892) 52 Fed. Rep. 671, following Morgan's L. & T. R. & S. S. Co. *v.* Texas Cent. Ry. Co., 137 U. S. 171; s. c., 11 Sup. Ct. Rep. 61.

[2] Gernsheim *v.* Olcott, (1889) 7 N. Y. Supp. 872. As to jurisdiction, see McBee *v.* Central Trust Co. of New York, 48 Fed. Rep. 243; affirmed by the U. S. Circuit Court of Appeals for the sixth circuit in McBee *v.* Central Trust Co. of New York, (1893) 57 Fed. Rep. 753.

by these lienors to be maintainable, although some of the defendants were non-residents of the district. The court's view of the matter was that while such a bill was an original bill within the meaning of that term as used in equity pleading, yet the suit in its essence was supplementary to the ancillary foreclosure suit which it sought to oppose, and hence the court's jurisdiction was unaffected by the fact that when the parties were arranged according to their interests in the suit, some who were residents of the same state would be found on opposite sides of the controversy.[1] A railroad company had been incorporated both in the state of Georgia and the state of South Carolina. The United States Circuit Court for the southern district of Georgia had appointed a receiver, and an ancillary suit was filed in the district of South Carolina to have his authority extended over the property of the company in that state. The complainant in the bill was a citizen of Georgia. Other citizens of Georgia were parties to the bill, which was the counterpart of the bill originally filed in Georgia, but no relief was asked against them. It was held upon a question of jurisdiction that the controversy was between citizens of different states, and the jurisdiction of the United States Circuit Court in South Carolina of the ancillary bill was maintained.[2] It appeared here that a railway company, the road of which passed through several states, purchased a small road lying entirely within one of the states. Afterwards it mortgaged the whole system, including the newly-purchased road. Several years afterwards there was brought in the Federal Circuit Court a suit to foreclose this general mortgage, and the whole property was placed in the hands of the receiver appointed in the federal court. The charter of this state road was, in the meantime, by proper proceedings in the state court, declared forfeited, and a receiver of its property appointed. Upon the petition of this state receiver to the federal court for possession, in which petition it was alleged that the sale of the road to the interstate company was *ultra vires* and void, and that, therefore, the federal court had no jurisdiction, it was held that this petition merely raised the question as

[1] McBee *v.* Marietta & N. G. Ry. Co., (1891) 48 Fed. Rep. 243.

[2] Phinizy *v.* Augusta & Knoxville R. Co., (1893) 56 Fed. Rep. 273. See as to the citizenship of the corporation, Shaw *v.* Mining Co., 145 U. S. 449; s. c., 12 Sup. Ct. Rep. 935; Railway Co. *v.* Whitton, 13 Wall. 283; Nashua & Lowell R. Corp. *v.* Boston & Lowell R. Corp., 136 U. S. 356; s. c., 10 Sup. Ct. Rep. 1004.

to the validity of the sale, which question could properly be tried in the federal court, and hence it would retain possession. Besides, the fact that the mortgagees of a prior mortgage, which was placed upon this state road before its order, had intervened in the federal court for the protection and enforcement of their prior lien, was also a sufficient ground for retaining jurisdiction and possession of the road. Nor did the fact that the state statutes provide for the payment of the corporation's debts after its charter is forfeited, and for the distribution of its assets, give the state courts exclusive jurisdiction, as these directions would be complied with in the federal courts.[1] In this suit for foreclosure in a state court of a corporation mortgage, one claiming the title to the property mortgaged by the corporation was made a party defendant; the claimant, as a non-resident, had the case removed to the federal court. In this court the case was ordered to be remanded on the ground that as in a suit for foreclosure only the rights and interests under the mortgage and subsequent to it could be determined, and that this third person who claimed a paramount and independent title was not a proper party to the suit, he should have applied to the state court where the foreclosure suit was proceeding for leave to bring an independent suit in that court against the receiver.[2] The following rules as to practice in foreclosure suits were declared in this case: A motion to consolidate three foreclosure suits when all are not ripe for decree, and where nothing can be gained for the purpose of a hearing, will be denied. Leave to file a cross-bill in a suit of foreclosure, where it appears that the purpose is to secure, between an alleged debtor and the mortgagor, an accounting not necessary to the determination of the suit, will be denied. Where a railroad is in the hands of receivers pending suits of foreclosure and settlement of the priority of liens, it is proper, on the application of a lienholder claiming priority, to extend the receivership as to such claim over the portion of the road on which the priority is claimed.[3] Here a mortgage bondholder sued for foreclosure in behalf of himself and all the other bondholders, and the other

[1] Mercantile Trust Co. *v.* Missouri, K. & T. Ry. Co., (1890) 48 Fed. Rep. 351.

[2] California Safe Deposit & Trust Co. *v.* Cheney Electric Light, Telephone & Power Co., (1893) 56 Fed. Rep. 257.

[3] Mercantile Trust Co. *v.* Missouri, K. & T. Ry. Co., (1889) 41 Fed. Rep. 8.

bondholders though not made parties, intervened by leave of the court, and prayed a foreclosure. It was held in the United States Circuit Court for the district of Washington that all such bondholders were indispensable parties, and in determining the jurisdiction of the court, they were all to be considered as parties plaintiff; and it having appeared that one of them was a citizen of the same state with several of the defendants, the jurisdiction of the federal courts failed.[1]

§ 535. **Bringing such actions — rules.**— A prior mortgagee cannot be required, against his will, at the instance of a subsequent mortgagee, to foreclose his mortgage.[2] In this case, the trust company, which was the trustee under a railroad mortgage, filed its bill in the United States Circuit Court for foreclosure of the mortgage as well as to set aside a sale of the railroad which had been made under a decree of the state court, in which proceedings it was charged there was fraud upon the part of the movers in the same. There being no averment in the bill that sixty per cent of the owners of the outstanding bonds had requested action on the part of the trustee, it was insisted that these proceedings were instituted without authority. The covenant in the mortgage upon which the contention was founded provided that in case of default, etc., in paying the interest and principal of the bonds, "it shall be the duty of the said trustees for the time being, and they shall or will, upon written request of the holders of sixty per centum of the said bonds then outstanding, enter upon and take possession of the said railroad property and estate," and operate the same, appropriating the net income to the best advantage, etc., "or the said trustee shall and will, after, or without entering upon or taking such possession, upon the written request of the holders of bonds of a like amount, proceed upon, and under this indenture of mortgage, to sell the railroad property and estate * * * at public sale in the city of Philadelphia, first giving at least four weeks' notice by publication, etc., and grant and convey the same to the purchaser, freed from all and every trust hereby created," etc. The

[1] Mangels *v.* Donau Brewing Co., (1892) 53 Fed. Rep. 513. See Removal Cases, 100 U. S. 468. The court distinguished Stewart *v.* Dunham, 115 U. S. 61; s. c., 5 Sup. Ct. Rep. 1163.

[2] Seibert *v.* Minneapolis & St. Louis Ry. Co., (1893) 52 Minn. 246; s. c., 53 N. W. Rep. 1151.

Supreme Court of the United States reversed the decree of the United States Circuit Court, dismissing this bill.[1] The court also held in this case that a provision in the railroad mortgage that the mode of sale provided by it "shall be exclusive of all others," was an attempt to provide against a remedy in the ordinary course of judicial proceedings and oust the jurisdiction of the

[1] Guaranty Trust & Safe Deposit Co. *v.* Green Cove Springs & Melrose R. R. Co., (1891) 139 U. S. 137; s. c., 11 Sup. Ct. Rep. 512. Mr. Justice BROWN, speaking for the court, referred to the case of Chicago, etc., R. R. Co. *v.* Fosdick, 106 U. S. 47, 77, which was claimed to be decisive of the question of authority to bring the action, as follows: "In that case, which was a bill for foreclosure, the proviso was that the trustee, upon the written request of the holders of a majority of the bonds then outstanding, should proceed to collect both principal and interest of all such bonds outstanding, by foreclosure and sale of said property or otherwise, as therein provided. It was argued that the office of this clause was merely to make the obligation of the trustees imperative instead of optional, but the court held that the whole article must be taken together as a unit, and 'the nature of the provision and the character of its object must be taken into consideration as furnishing the rule of its interpretation.' It will be observed, however, that the provision was directed against the very proceeding taken by the trustees in the suit, namely, a foreclosure and sale of the property; while in the present case it is directed only to a taking possession or a sale *under the deed of trust* without institution of legal proceedings. A case nearer in point is that of Morgan's Steamship Co. *v.* Texas Central Railway, 137 U. S. 171, decided at the present term, in which the condition was that on default continuing for sixty days in the payment of interest or any part of principal, the principal of the bonds should become immediately due, and that upon request of seventy-five per cent of the holders of bonds and written notice of the same, the trustee should take possession of the property and operate it for the benefit of the bondholders, and that upon like request he should proceed to foreclose the mortgage and sell the property to the highest bidder for cash. It was also provided that nothing contained in the instrument should be construed to prevent or interfere with the foreclosure by any court of competent jurisdiction. It was held that the trustee could maintain a bill to foreclose the mortgage upon occurrence of a default without averring or proving a request of seventy-five per cent of the bondholders, as such request was necessary only in case the trustee wished to proceed to foreclose or take possession *ex mero motu* without the intervention of a court. We think that such limitations upon the power of the trustee to take legal proceedings to enforce payment of the amount secured should be strictly construed. In this case the condition only relates to the taking possession of the property under the deed of trust, or to a sale in the city of Philadelphia under the power of sale contained therein, and we think it should not be held to apply to foreclosure proceedings begun in a court of competent jurisdiction to obtain a judicial sale of the property. This was the ruling in the eighth circuit by Judge DILLON

courts, and was, therefore, invalid.[1] A mortgage of railroad property to a trustee to secure bonds and interest coupons, with provision that in case of demand and default of payment of interest for six months the trustee may enter upon the property, with a similar provision as to advertisement and sale, with an article besides stipulating that both of those remedies were cumulative of foreclosure proceedings in the courts which the trustee should institute at the direction of the bondholders "upon default being made as aforesaid," authorizes a bill to foreclose, although the default has not continued six months.[2] It was urged in abatement of this suit to foreclose a mortgage executed by a railroad company, that it was prematurely brought because default in the payment of interest had not continued for six months. The contention was based upon the language of the article in the trust deed which read as follows: "It shall be the duty of the trustee, upon a requisition in writing, signed by the holders of not less than one-quarter in amount of the said bonds then outstanding, and upon adequate security and indemnity against all costs, expenses and liabilities to be by the trustees incurred, to proceed to enforce the rights of the bondholders under this indenture, either by the exercise of the powers granted by articles 9 and 10 of this indenture, or of any of said powers, or by a suit or suits in equity or at law in aid of the execution of such powers,

in Alexander *v.* Central Railroad of Iowa, 3 Dill. 487, and by Judge CALDWELL in Credit Co. *v.* Arkansas Central Railroad Co., 15 Fed. Rep. 46, and we think it is sound. * * * Again, it is evident that this was a condition for the benefit of the grantor and its assigns, and that intervening lienholders and those who have purchased the property under decrees in their favor do not stand in a position to take advantage of this covenant. The whole object of the covenant was to protect the mortgagor against a seizure and sale of its property for non-payment of interest or principal at the mere caprice of the trustee, or without the consent of a majority of the stockholders, and it has no application to a case where the mortgagors have already lost the property under adverse proceedings instituted by parties having no connection with the mortgage."

[1] Guaranty Trust & Safe Deposit Co. *v.* Green Cove Springs & Melrose R. R. Co., (1891) 139 U. S. 137; s. c., 11 Sup. Ct. Rep. 512; citing Hope *v.* International Society, 4 Ch. D. 327; Edwards *v.* Aberayron Ins. Society, 1 Q. B. D. 563; Horton *v.* Sayer, 4 H. & N. 643; Scott *v.* Avery, 8 Exch. 487; s. c., 5 H. L. Cas. 811; Thompson *v.* Charnock, 8 T. R. 139; Mitchell *v.* Harris, 2 Ves. Jun. 129; Tobey *v.* County of Bristol, 3 Story, 800; Noyes *v* Marsh, 123 Mass. 286; King *v.* Howard, 27 Mo. 21; Conner *v.* Drake, 1 Ohio St. 166; Trott *v.* City Ins. Co., 1 Cliff. 439; 2 Story Eq. § 1457.

[2] Mercantile Trust Co. *v.* Missouri, K. & T. Ry. Co., (1888) 36 Fed. Rep. 221.

or otherwise, as the trustee, being advised by counsel, shall deem most effectual to enforce such rights." Article 9 treated of the rights of the trustee to enter and operate the road in case of default in payment of interest continuing for six months. Article 10 treated of the rights of the trustee to enter and sell in case of default of the principal of the bond. The federal court held that the trustee was not deprived by the provisions of the right, in its discretion, to begin foreclosure proceedings immediately upon default in the payment of interest.[1]

§ 536. **Parties to such actions.**— The trustee named in a corporation mortgage or deed of trust, holding title for all the bondholders as beneficiaries, is the proper party to institute foreclosure proceedings, but in case of unreasonable neglect, or a refusal to discharge his duty, any bondholder may bring an action to enforce his security for the common benefit.[2] The United States Circuit

[1] Farmers' Loan & Trust Co. *v.* Chicago & Northern Pac. R. Co., (1894) 61 Fed. Rep. 543. JENKINS, Circuit Judge said: "This provision, as I conceive, has only reference to the exercise of the powers granted by articles 9 and 10, and to proceedings in aid of the execution of such powers. It is, moreover, mandatory, rendering action by the trustee imperative when the requisite number of bondholders shall require it, to act upon completion of the stipulated period of default. It does not interfere with the exercise of discretion of the trustee to act or limit its right to act immediately upon default. This view is strengthened by the subsequent provision declaring that the rights of entry and sale are granted or intended as cumulative remedies additional to all other remedies allowed by law, and that the same shall not be deemed in any manner whatsover to deprive the trustee or the beneficiaries under the trust of any legal or equitable remedy by judicial proceedings consistent with the provision of the trust deed. The subsequent provisions in prevention of suit by individual bondholders, without first giving notice in writing to the trustee of default continued for six months, and requesting it, to institute suit, are simply restraints upon the action of individual bondholders in supposed antagonism to the interests of the bondholders in a body. I think this case falls within the principle of Railroad Co. *v.* Fosdick, 106 U. S. 47; s. c., 1 Sup. Ct. Rep. 10; Morgan's L. & T. Railroad & Steamship Co. *v.* Texas Cent. Ry. Co., 137 U. S. 171; s. c., 11 Sup. Ct. Rep. 61; Farmers' Loan & Trust Co. *v.* Winona & S. W. Ry. Co., 59 Fed. Rep. 957. While it is true that a mortgagor has the right to stipulate for a breathing spell for the payment of his matured debt, it is still true that the limitations upon the powers of the trustee to take the legal proceedings to enforce payment upon default should be strictly construed. Guaranty Trust & Safe Deposit Co. *v.* Green Cove Springs & Win. R. Co., 139 U. S. 137; s. c., 11 Sup. Ct. Rep. 512."

[2] Seibert *v.* Minneapolis & St. Louis Ry. Co. (Griggs, Intervener), (1893)

Court of Appeals for the fifth circuit has held a foreclosure suit properly brought by one of three trustees named in the trust deed, where he averred that one of the other trustees was dead, and that the remaining one, who was made a defendant at a sale of the property covered by the trust deed under a decree of the state court, claimed to be interested in the purchase thereof, and was "interested adversely to the complainant as trustee of the bondholders."[1] They also held that the trustees, being empowered in this trust deed, on default of interest payments, to sell the property, "if, after notice is served on the president of said company, the same shall remain unpaid for six months after such default," having sued to foreclose, instead of selling under the power, it was unnecessary to aver the giving of notice of default to the president of the corporation.[2] The Supreme Court of New York, sitting in another department, having before it proceedings to declare the insolvency of and appoint a receiver for a trust company which had been named as trustee in a trust deed executed by a corporation to secure bonds which it had issued, upon motion of bondholders appointed another trust company trustee for the holders of said mortgage to fill the vacancy occasioned by the insolvency of the trustee first named, disabling it to act any longer in that capacity. This newly-appointed trustee brought action for foreclosure of the mortgage, and in the foreclosure action the legality of the appointment of the trustee to fill the vacancy was questioned, as not being within the terms of the provision as to filling such vacancy in the trust deed. The Supreme Court of New York, in General Term, held that the Supreme Court, succeeding to the jurisdiction and power of the old Court of Chancery, had jurisdiction of trusts and trustees, and had power, independent of any statute, to remove a trustee, on good cause shown, and to appoint another in his place; that the original trustee, under the trust deed, becoming insolvent, that court had jurisdiction to appoint a successor trustee. They further held that this trustee, having been accepted by the mortgagee and the bondholders as satisfactory, as evidenced by the action of

52 Minn. 148; s. c., 53 N. W. Rep. 1134.

[1] Alabama & Georgia Manufacturing Co. *v.* Robinson, (1893) 56 Fed. Rep. 690, affirming Robinson *v.* Alabama & Georgia Mfg. Co., (1891) 48 Fed. Rep. 12.

[2] Alabama & Georgia Manufacturing Co. *v.* Robinson, (1893) 56 Fed. Rep. 690.

those parties in the proceedings throughout, the mortgagee executing a supplemental mortgage to this trustee, and the bondholders placing their bonds under the control of the trustee, for receiving payments of interest, and for final action for foreclosure of mortgage, a stranger, not a trustee, could not raise any question as to the jurisdiction of the court appointing the successor trustee, or as to the regularity of the proceedings.[1] In this case the trust company, acting as trustee for bondholders under the mortgage, through its secretary, sent notice to the corporation mortgagor that it exercised the option given in the mortgage to declare the principal of the bonds due after the lapse of a fixed time in not relieving the default as to the payment of the interest. The Supreme Court of New York, in General Term, held that there was no necessity for a resolution of the directors of the trust company directing the secretary to take this action; that it was a matter that called for no deliberation or action upon the part of the directors; that it was a mere executive duty, which the executive officers of the trust company could perform in the ordinary discharge of their duty. It had been requested to take this action by the majority of the bondholders, and by the terms of the mortgage the request by the bondholders was conclusive and mandatory. Besides, the bringing of the suit of foreclosure was a sufficient declaration of the intention of the trustees to exercise the option.[2] The provision in a railroad mortgage that the trustees, after default and upon petition of the owners of a certain amount of the bonds, may take possession of and manage the road, or sell it, at their option, does not affect the right of the trustees as legal owners of the mortgage to go into a court of equity after default and ask the appointment of a receiver and foreclosure of the mortgage, without waiting for any action upon the part of the bondholders.[3] When a mortgage is made to a trustee to secure coupon bonds, the right to bring suit of foreclosure is in the trustee, which right,

[1] New York Security & Trust Co. *v.* Saratoga Gas & Electric Light Co., (1895) 34 N. Y. Supp. 890.

[2] Ibid.; citing Bank *v.* Kidder, 106 N. Y. 221; s. c., 12 N. E. Rep. 577.

[3] Phinizy *v.* Augusta & Knoxville R. Co., (1893) 56 Fed. Rep. 273. As to what provision in a mortgage for entry and possession by the trustee did not preclude the trustee from his regular action for foreclosure of mortgage for a default as to payment of interest, see Farmers' Loan & Trust Co. *v.* Winona & S. W. Ry. Co., (1893) 59 Fed. Rep. 957.

however, is not exclusive of the bondholders, unless made so by terms of the deed. And where a trustee in a mortgage securing coupon bonds accepts the position of trustee in a subsequent deed of general assignment made by the mortgagor for the benefit of all its creditors, which embraces the property covered by the mortgage, the respective interests to be represented by the trustee under the deed being conflicting and antagonistic, such acceptance on the part of the trustee would cause a forfeiture of any preference the trustee might otherwise have had, as against the bondholders, to bring suit to foreclose the mortgage.[1] The trust deed given to secure an issue of a New Jersey corporation's bonds, after conferring on the trustee a right to enter and hold possession, to sell, etc., declared that those remedies were merely cumulative, and additional to all other remedies allowed by law, and that the same should not be deemed to deprive the trustee, "or the beneficiaries under the deed," of any legal or equitable remedy. The whole series of bonds was to become due upon a default for six months in the payment of the interest. The mortgage was upon property of the corporation situated in Louisiana. A suit for foreclosure of this mortgage upon a default for the six months as to the interest was brought by a bondholder in the federal court for the eastern district of Louisiana. It was held, upon objection to the suit by a bondholder, that where the position of trustee was vacant, this owner of a majority of the bonds was entitled to maintain his suit in the federal court in his own name to foreclose the mortgage for himself and the other bondholders, and that the court would not compel him to go to New Jersey to have another trustee appointed.[2] Where there is a provision in a mortgage made to a trustee to secure coupon bonds that, in case of non-payment of any one of the bonds or coupons for thirty days after maturity, and payment demanded, it would be lawful for one-fifth or more of the holders of the bonds to cause the principal to be at once matured, and to call on the trustee to foreclose the mortgage, the bondholders alone are to exercise

[1] American Tube & Iron Co. *v.* Kentucky Southern Oil & Gas Co, (1892) 51 Fed. Rep. 826, overruling a demurrer to the bondholders' suit to foreclose.

[2] Wheelwright *v.* St. Louis, N. O. & O. Transportation Co., (1893) 56 Fed. Rep. 164. The court calls attention to Railroad Co. *v.* Orr, 18 Wall. 471, and Railroad Co. *v.* Fosdick, 106 U. S. 47; s. c., 1 Sup. Ct. Rep. 10, distinguishing them.

the option. The trustee need not join with them.[1] Where a mortgagor corporation and the trustee of the mortgage are citizens of the same state, the holders of bonds secured by the mortgage cannot bring suit in a federal court to foreclose the mortgage in their own name, without showing reasons why the suit is not brought by the trustee.[2] Mortgage bondholders, upon default in the payment of their bonds, may properly institute a foreclosure suit where a railroad company has been sued by a few minority stockholders, and a receiver asked, the suit being opposed by a great majority of the stockholders, and have a receiver appointed and thus control any litigation which might withdraw from the corporation the mortgaged property; and it would not be fraudulent or collusive for the officers of the corporation to admit the truth of the allegations in the bill filed by the bondholders. And a stockholder who has brought such a suit against the corporation cannot, by intervening in the bondholders' suit to foreclose, have such suit stayed until his suit is determined, unless the case be an extraordinary one, and such a proceeding be justified within sound judicial discretion.[3] The prayer of a petition of a committee representing bondholders under various mortgages of railroads, to be made a party plaintiff in a foreclosure suit where a receiver had been appointed for the property of a railroad company which owned or controlled a large number of other roads operated under separate charters, was denied in the United States Circuit Court for the eastern district of Virginia, the court holding that the fact that a single trust company was trustee under twelve different mortgages or trust deeds was not of itself a sufficient ground to support the petition, in the absence of anything showing negligence on the part of the trustee in protecting the interest of the bondholders or that there was any conflict between the various interests represented by the trustee.[4] One seeking to enforce by

[1] American Tube & Iron Co. *v.* Kentucky Southern Oil & Gas Co., (1892) 51 Fed. Rep. 826.

[2] Needham *v.* Wilson, (1891) 47 Fed. Rep. 97.

[3] Pennsylvania Co. for Insurance of Lives and for Granting Annuities *v.* Jacksonville, T. & K. W. Ry. Co. (American Construction Co., Intervener), (1893) 55 Fed. Rep. 131.

[4] Clyde *v.* Richmond & Danville R. Co., (1893) 55 Fed. Rep. 445. GOFF, Circuit Judge, said: "I think the rule is now well established that the individual bondholder and the separate beneficiary will not be made parties to suits relating to the mortgage or trust deed unless it is alleged and shown that the trustee is incompetent, or for some reason cannot faithfully repre-

suit a specific lien which does not involve the validity of a trust deed of a corporation, or affect its lien, when all the bondholders are before the court, and the joinder would oust the jurisdiction, need not join the trustee of the corporation trust deed or mortgage as a party defendant.[1] There was a petition in this suit to foreclose a railroad mortgage in which the petitioners prayed that they be allowed to be made parties defendant, alleging as a reason that the defendant company was made up by an illegal consolidation of three other companies, in one of which the petitioners were stockholders; that they never consented to, or recognized the validity of, the consolidation, and were not bound by it or by the act of the new company creating the mortgage; that the new company was "perhaps concluded by its conduct in the premises from making defense" to the suit; that the original company, of which they were stockholders, had no officer or representative upon whom they could call to make defenses for them, and that the counsel for the consolidated company declined to set up the defense which they desired to make. It was held by the United States Circuit Court for the northern district of Georgia that the facts stated in the petition gave no right to these petitioners to intervene as defendants, especially as there was no charge of fraud or collusion, and the proper remedy was by an independent suit.[2]

§ 537. **General rules as to such actions.**— In case the trustee in the junior of a series of mortgages pledging income of the railroad company and a stipulation in case of default in interest for the taking of possession of the property by the trustee, brings an action to foreclose his mortgage, making the prior mortgagees parties defendant, and obtains the appointment of a receiver to take possession of and operate the railroad and receive its earnings, the senior mortgagees may apply to the court to have the

sent the *cestui que trust.*" The following cases will be found of interest upon this question: Skiddy *v.* Railroad Co., 3 Hughes, 320; Wetmore *v.* Railroad Co., 1 McCrary, 466; s. c., 3 Fed. Rep. 177; Railroad Co. *v.* Howard, 7 Wall. 392; Richter *v.* Jerome, 123 U. S. 233; s. c., 8 Sup. Ct. Rep. 106; Shaw *v.* Railroad Co., 5 Gray, 162; Farmers' Loan & Trust Co. *v.* Kansas City, W. & N. W. R. Co., 53 Fed. Rep. 182; Van Vechten *v.* Terry, 2 Johns. Ch. 197; Kerrison *v.* Stewart, 93 U. S. 155; Richards *v.* Railroad Co., 1 Hughes, 28.

[1] Holly Mfg. Co. *v.* New Chester Water Co., (1891) 48 Fed. Rep. 879.

[2] Central Trust Co. of New York *v.* Marietta & N. G. R. Co., (1891) 48 Fed. Rep. 14.

receiver hold for and pay to them so much of the net earnings as is covered by their mortgages, and are, therefore, entitled to receive the same.[1] There was here a cross-bill filed by the trustees of a first consolidated railroad mortgage, after declaring the mortgage due before maturity for default in interest, pursuant to the

[1] Seibert *v.* Minneapolis & St. Louis Ry. Co., (1893) 52 Minn. 246; s. c., 53 N. W. Rep. 1151. The court said: "But suppose the case of an action to foreclose by a junior mortgagee, and appointment, upon his application, of a receiver to take possession of the property and receive the income for his benefit only, while there were senior mortgagees having the right to take and hold possession and receive such income, we can easily conceive that if they acquiesce in the possession of the property and the receipt of the income by the receiver for purposes other than their mortgages, making no move towards asserting their claims, they would have no right to any part of the income any more than had they permitted the mortgagor to remain in possession and to receive and disburse it for its general purposes. Such was the case of Sage *v.* Memphis & L. R. R. Co. 125 U. S. 361; s. c., 8 Sup. Ct. Rep. 887, in which the mortgagees had laid by until all the moneys they sought to have paid to them had been earned by the receiver, and he had been discharged. The purpose of that action was only to satisfy the plaintiff's claim, and for that purpose the receiver was appointed and the income was earned; but the purpose of this action is, in part at least, to adjust the rights of all the parties, as well to the income as to the body of the property. For the purpose of adjusting their rights to the income it was necessary for the court to lay hold upon, not merely that portion which the plaintiff might be entitled to, but that which all the parties were entitled to. The order appointing the receiver not assuming to appropriate it to plaintiff, the court was to be regarded as taking and holding it for all the parties, as their rights and interests might appear, at least so long as none of them made objection. * * * Being unable to take the possession from the mortgagor, or from the receiver, what then can [senior mortgagees of income] do, except, if they are not parties to the action, to come in by intervention, or, if they are parties, to petition the court that there be paid to them by the receiver out of the earnings which shall come into his hands such part as, but for his appointment, they would have had the right to receive and apply on their mortgages? The right of the prior mortgagees to take such a way to assert their claim, and subject the earnings to their lien, was recognized in the Sage case, the court saying: 'There was no moment pending the receivership when these parties, upon the request of the holders of a majority of the bonds, might not have appeared in this suit, or in a separate suit, in the same court, and asked that the receiver hold for them as well as Sage, or that he be discharged, and they be put into possession of the mortgaged property for the purpose of sale pursuant to the mortgage.' When such mortgagees are in the action, and so in a position to make their demand upon the court, it is entirely immaterial in what form it is made, so that it is clearly made, and presents to the court the ground of their claim, if it be not already before it."

terms of their mortgage in a pending foreclosure suit brought by second consolidated mortgage bondholders, which also prayed a foreclosure. Other lienors praying for a sale also came into the suit, their liens being prior to the first consolidated mortgage and past due. After this a cross-bill was filed by a majority of the holders of the bonds secured by the first consolidated mortgage, in which they repudiated the action of their trustees declaring the mortgage due, and prayed the court to order a sale subject to all incumbrances prior to the second consolidated mortgage, and to direct the payment out of the proceeds of all arrears of interest on the bonds secured by the first consolidated mortgage, and on certain mortgages prior to that, not offering, however, to bid an amount sufficient to pay these arrearages, or any of the large costs and expenses of the suit. The United States appellate court held that the Circuit Court rightfully refused to decree as requested in this cross-bill of the bondholders, and properly adhered to its determination to decree a sale free of all liens, reserving a right to any party to redeem on paying the several amounts found due, with costs.[1] There should be in a petition of junior lienors to be allowed to redeem prior mortgages, in foreclosure proceedings, an offer to pay whatever sums the junior lienors admit to be due. A prayer in such a petition that the prior mortgagees be required to deposit their securities in court in order that the petitioners "may have the privilege of redeeming" them has been held by the United States Court of Appeals to be insufficient.[2] A railroad company operated a road which with the property connected was located partly in the state of Ohio and partly in the state of Indiana. There had been a foreclosure of a mortgage upon this road and property in a state court of Ohio. A bondholder instituted his suit afterwards in the United States Circuit Court for the district of Indiana against the company and the trustee named in the mortgage, alleging that the trustee refused to bring action for foreclosure of the mortgage as against the property situated in that state. The decree in foreclosure in Ohio was pleaded in bar of the suit. The federal court held the plea insufficient, on the ground that under such circumstances a court of one state cannot merge into its judgment the lien on the property in the other state, and, while it may act upon

[1] Bound *v.* South Carolina Ry. Co., (1893) 58 Fed. Rep. 473.

[2] Ibid.

the person of defendant so as to compel it to make conveyances or releases, yet, if it had not done so, its mere judgment was not a bar to a suit in the other state between the same parties to foreclose the same mortgage there.[1] The trustees of railroad mortgage bondholders represent their bondholders in any litigation relating to the trust,

[1] Lynde *v.* Columbus, C. & I. C. Ry. Co., (1893) 57 Fed. Rep. 993. It was said in the opinion: "It is argued that, in respect of immovable property mortgaged by an interstate railway, a different rule has been established by the case of Muller *v.* Dows, 94 U. S. 444. It is contended that the court there held that as the railroad and its franchise were an entirety, any court having jurisdiction of the parties and subject-matter could make a valid decree of foreclosure which would operate on the entire railroad property as well without as within the state where the decree was procured, and that it would completely merge the lien of the mortgage. What was there said giving apparent support to this contention was merely *arguendo*, and was not essential to the judgment pronounced. In that case the Circuit Court of the United States for the district of Iowa passed a decree of foreclosure and sale of a railroad extending from a point in Iowa to a point in Missouri, and owned by a corporation formed by the consolidation of a corporation of Missouri with a corporation of Iowa. The entire line was covered by one trust deed, and the suit to foreclose was brought by the trustee. The mortgagees were also before the court, and the sale was made by a master at the instance of the trustee. It was held that the decree was not void so far as it directed the foreclosure and sale of that part of the railroad lying in Missouri, and that the trustee could be required by the court in Iowa to make a deed to the purchaser in confirmation of the sale. In my judgment this case does not overturn the well-established doctrine that a court in one state cannot pass a decree which shall operate to change the title to or merge a lien upon immovable property in another state. The title in that case was transferred by the court compelling the execution of a power of sale, and not by force of the decree. Mercantile Trust Co. *v.* Kanawha & O. Ry. Co., 39 Fed. Rep. 337; Farmers' Loan & Trust Co. *v.* Postal Telegraph Co., 55 Conn. 334; s. c., 11 Atl. Rep. 184. The case last cited is exactly in point. The Postal Telegraph Company, a New York corporation, mortgaged all its property, which was situated in several states, including Connecticut and New York, to the plaintiffs, in trust, to secure the payment of its bonds. Upon a failure to pay the interest the plaintiffs brought a suit for a foreclosure in the Supreme Court in the city of New York. Judgment was rendered for the plaintiffs, pursuant to which a referee was appointed, who sold all the property, including the real estate in Connecticut, and executed a conveyance of the same to the purchaser. Suit was brought to foreclose the mortgage on the Connecticut property according to the laws and practice in that state. The defendant, * * * an attaching creditor, appeared and set up a special defense, alleging the foreclosure and proceedings in the state of New York. The defense was held insufficient on the ground that the decree and proceedings had thereunder were nugatory as to the real estate situate in Connecticut."

and where the purpose of the suit is substantially the same as a foreclosure of the mortgage, the fact that the trustee is a party defendant instead of plaintiff is immaterial, and the bondholders are bound by the decree, although they may not be parties to the suit.[1] An intervening petition in proceedings to foreclose railroad mortgages, filed by one claiming under a contract for the purchase of land from the land agent of the company, where it appeared that the land in question, together with other lands, was specially excepted by the orders appointing the receiver from the property thereby put into his hands, and that he had never come into possession of the lands, and that in none of the several causes was there any controversy about the lands, nor any declaration of lien thereon in the respective decrees, and the intervener and the defendant company were citizens of the same state, was held by the United States Circuit Court to have been properly dismissed, both as thrusting a foreign litigation into the suit and for want of jurisdiction.[2]

[1] Pollitz *v.* Farmers' Loan & Trust Co., (1892) 53 Fed. Rep. 210. COXE. D. J., said: "In Shaw *v.* Railroad Co., 100 U. S. 605, the Supreme Court says: 'The trustee of a railroad mortgage represents the bondholders, and all legal proceedings carried on by him affecting his trust, to which they are not actual parties, and whatever binds him, if he acts in good faith, binds them. * * * The trustee represents the mortgage, and in executing his trust may exercise his own discretion within the scope of his powers.' In Beals *v.* Railroad Co., 133 U. S. 290; s. c., 10 Sup. Ct. Rep. 314, the court said: 'The former judgment was rendered by a court of competent jurisdiction, to which not only the railroad company that issued the bonds, but the surviving trustee under the mortgage made in the name of another company to secure the payment of those bonds, were made parties. The bondholders were thus fully represented in that suit, and bound by the decree canceling and annulling the bonds and mortgage, unless the decree was fraudulently obtained.' See, also, Kent *v.* Iron Co., 144 U. S. 75; s. c., 12 Sup. Ct. Rep. 650; Richter *v.* Jerome, 123 U. S. 233; s. c., 8 Sup. Ct. Rep. 106; Bank *v.* Shedd, 121 U. S. 74; s. c., 7 Sup. Ct. Rep. 807; Elwell *v.* Fosdick, 134 U. S. 500; s. c., 10 Sup. Ct. Rep. 598. These authorities, in my judgment, are conclusive."

[2] Cutting *v.* Florida Ry. & Nav. Co. (Wilson, Intervener), (1891) 45 Fed. Rep. 444. As to the right of the trustee to foreclose upon default in the payment of interest and to have a receiver appointed, see Mercantile Trust Co. *v.* Chicago, Peoria & St. Louis Ry. Co., (1893) 61 Fed. Rep. 372. That the provision in a mortgage for an entry by the trustee of the mortgage in case of default in interest for twelve months, will not prevent a foreclosure of the mortgage for interest past due, see Central Trust Co. *v.* New York City & Northern R. R. Co., 33 Hun, 513. When bondholders not wishing a foreclosure should be allowed to stop proceedings, see Tillinghast *v.* Troy & B. R. R. Co., 1 N. Y.

§ 538. **Decrees in such actions — general rules.**— In a proper case, a court of equity has the power so to mould its decree as to order a sale of the mortgaged premises to satisfy that part of the mortgage debt which is due, and preserve the lien upon the mortgaged premises in the hands of the purchaser as to the unmatured part of the debt. In this case a railroad company negotiated its coupon bonds, secured by a mortgage upon its railroad, etc., each bond having an indorsement by another railroad company, binding it to purchase at maturity the bond and each interest coupon at par, "and, when so purchased, each and all of said bonds and coupons are to be held by the said company, with all the rights thereby given and with all the benefit of every security therefor." The guaranty company, having been obliged to purchase coupons, filed a bill before the maturity of the bonds. It was held by ACHESON, J., in the Circuit Court for the western district of Pennsylvania, that the contract of purchase must be so construed as to preserve to the bondholders their mortgage lien until the guaranty company should have fully performed its obligations according to the tenor of its indorsement, and that in the meantime its remedies upon purchased coupons must be kept within such limits as would effect that object. The court in the case, therefore, deeming it settled that the equities of all the parties in interest would be best subserved by a sale of the railroad, etc., under and subject to the lien of the mortgage securing the bondholders as to the principal of the bonds thereby secured, and the interest payable after the making of the sale, so decreed.[1] The United States Supreme Court has held that, where the report of a master in a suit in equity to foreclose a railroad mortgage to whom it had been referred to take proof of the claims, found as to a bondholder that his bonds were due and unpaid; that certain coupons had been paid, and that certain other subsequent coupons had been made, but made no mention of the intervening coupons, and no exception taken to the report, it was a reasonable inference that the bondholder did not offer these intervening coupons in proof, and that the failure to find as to them could not be urged as an objection to the final decree.[2] Where

Supp. 243. When the silence of bondholders may be considered equivalent to an assent to a foreclosure of a mortgage, see Barnes *v.* Chicago, Milwaukee, etc., Ry. Co., 122 U. S. 1.

[1] Pennsylvania R. Co. *v.* Allegheny Valley R. Co., (1891) 48 Fed. Rep. 139.

[2] Coghlan *v.* South Carolina R. R. Co., (1891) 142 U. S. 101; s. c., 12 Sup. Ct. Rep. 150.

a railroad has been mortgaged to secure bonds which have been guaranteed by the state, a decree that a certain branch of the road is not subject to the mortgage lien, is of no validity when made in a suit in which the bondholders are not represented, and of which the state has not been notified, and which is brought in a county in which no part of such branch road is situated.[1] Upon a motion to make absolute the order confirming the sale of railway property in this foreclosure suit, the United States Circuit Court for the southern district of Alabama held, upon the question of its jurisdiction to hear and decide this motion, that an appeal and supersedeas did not oust the jurisdiction of the lower court, or preclude collateral or independent proceedings, and that this court was not precluded by an appeal and supersedeas of a decree in respect to solicitors' fees in this foreclosure proceeding from passing on the question of confirmation of the sale made under that decree. There being an objection to confirmation of this sale, that the price was inadequate, it was held that inadequacy of price alone was not a ground to set aside a judicial sale, unless so great as to shock the conscience and excite the suspicion of the court; that an expression of a well-founded opinion by a witness, that the property would on resale bring a much higher price, was not sufficient ground for setting aside such a sale. And while inadequacy of price, accompanied by additional circumstances of unfairness, growing out of fraud, accident or some trust relation, are good grounds against confirmation, the fact that mortgage bondholders of the company were known to have authorized a committee to bid up to $400,000, and that the report deterred others from bidding, was not good ground for setting aside a sale of the property for $225,000 to the bondholders.[2] The creditors of a railroad company and the mortgagor company itself consenting to the entry of a decree of foreclosure of the mortgage and sale of the railroad, without fraud, in pursuance of a plan of reorganization, such a decree will not be set aside at the suit of some of the stockholders merely because the principal of one mortgage was not yet due, should it appear that the sums due for interest on that mortgage, for floating indebtedness, and on other mortgages then due are so great as to render fore-

[1] Central Trust Co. *v.* Florida Ry. & Nav. Co. (Hawkins, Intervener), (1890) 43 Fed. Rep. 751.

[2] Fidelity Trust & Safety Vault Co. *v.* Mobile Street Ry. Co., (1893) 54 Fed. Rep. 26. See Mining Co. *v.* Mason, 145 U. S. 349; s. c., 12 Sup. Ct. Rep. 887.

closure inevitable, and in that case to deprive the stockholders of all their equity in the property, especially when the shareholders do not offer to do equity by paying the floating debt and have not been diligent in attacking the plan of reorganization or in attacking the decree complained of.[1] It appeared here that this insolvent railroad company had issued several series of bonds secured by mortgages, some of which mortgages covered all of its property and others only part. The principal of some of the bonds was due, and the company had defaulted on the interest on all of them. In addition it had a large floating debt, running into millions. There was no fair possibility of its being able to pay the accrued interest on the bonds and the floating debt without sale of all its properties. Certain stockholders filed their bill to set aside a decree of foreclosure of the mortgages and to enjoin the defendants from carrying out the plan of reorganization. The United States Circuit Court held that this decree of foreclosure, entered by consent of the creditors, would not be set aside at this suit of the stockholders on the ground that the principal of some of the mortgages was not yet due, as it was to the interest of the railroad company that the rights of all the mortgage bondholders should be cut off to enable the company to effect a reorganization which would secure and extend its bonded debt and reduce the rate of interest thereon and provide the necessary means to satisfy the floating debt. Nor would a proposed reorganization of the company, to be effected in connection with the foreclosure sale, by which the bonded indebtedness was to be refunded on longer time and at reduced interest, and each stockholder being allowed to retain his stock on the payment of his *pro rata* share of the floating debt, it not being a fraud on the stockholders, be enjoined at the suit of some of the stockholders who did not suggest any other method by which the financial embarrassments of the company could be met.[2] A final decree for foreclosure of railroad mortgages directed that the property be sold subject to any and all liens prior to the lien of the mortgages, and which had not been ascertained and adjudicated, and subject to receivers' certificates before that time authorized, and declared the certificates a first and prior lien on the property as between them and the mortgagees. The sale having taken place under

[1] Carey *v.* Houston & Texas Central Ry. Co., (1892) 52 Fed. Rep. 671.

[2] Carey *v.* Houston & Texas Central Ry. Co., (1891) 45 Fed. Rep. 438.

this decree, a decree was made upon the intervening claim of a mechanic's lien on part of the property presented before the receivers' certificates were authorized, allowing the mechanic's lien as a subsisting first lien on the property and directing payment of the amount by the purchaser and, on default, a sale of the property. This decree was affirmed on appeal by the Supreme Court. A holder of receiver's certificates brought a suit against the holders of this mechanic's lien for an injunction to restrain the enforcement of this decree. The United States Circuit Court of Appeals for the fifth circuit held that the enforcement of the decree ordering payment of this mechanic's lien could not be restrained by holders of the receiver's certificates claiming privity over it, they being bound by the decree as privies, and because an injunction for such a purpose in effect stayed execution of the final decree of the Supreme Court.[1]

§ 539. **Decrees for sale of property.**— It is proper upon foreclosure of a mortgage upon the property of a manufacturing corporation, to direct that the property be sold as an entirety, where it appears that a division of it into parcels would lessen its selling value.[2] Creditors claiming to have prior rights to the property of an insolvent corporation have no right to complain of a decree for the sale of the property of the corporation to satisfy a mortgage where such decree expressly provides that such creditors may present their claims to the court for adjudication before distribution of the proceeds of the sale.[3] It appearing in a suit to foreclose a mortgage given by a street railroad company to secure payment of certain bonds, that the bonds were invalid, still, as all the property covered by the mortgage was in possession of a receiver appointed pending the litigation, who

[1] Gordon *v.* Newman, (1894) 62 Fed. Rep. 686. WHITE, Circuit Justice, said: "That the holders of receiver's certificates depend for their ultimate rank upon the final decree in the cause where the certificates are issued is beyond question." A text book thus states the rule: "The holders of these securities must see to it that in the order distributing the purchase money the proper provision is incorporated for their redemption, because, if once the property is sold, and the court makes a final decree without providing for the payment of the certificates, there is an end of the matter. * * *" Beach Rec. par. 401, p. 332; citing, also, Mercantile Trust Co. *v.* Kanawha & Ohio Ry. Co., 58 Fed. Rep. 11; s. c., 7 C. C. A. 3.

[2] Central Trust Co. of New York *v.* United States Rolling Stock Co., (1893) 56 Fed. Rep. 5.

[3] Ibid.

had issued certificates for expenses incurred for the preservation of the property, a decree was entered, upon consent of all parties in interest, ascertaining and fixing the amounts of their respective claims, and directing a sale of all the property of the company to satisfy the same. The court held that rails, fish plates and bolts purchased by the company for use on its road, but which had not been actually used and were stacked upon land not within the company's right of way, were within the terms of the mortgage, which included all real and personal property of every kind and description, "used or intended to be used in connection with or for the purpose of said railroad," and came clearly within the decree. In the receiver's inventory of property of the railway company taken possession of by him under order of the court were set out certain notes, secured by mortgage, which had been executed to the railway company by a land association, and these notes were in the receiver's hands at the time of making the decree by consent for the sale of all the company's property. The court held that, even though these notes and mortgages securing them were not included in the railway mortgage sought to be foreclosed, as they had been brought into the custody of the court under color of its authority, and all parties in interest were parties to the suit, the court had jurisdiction to decide all conflicting rights thereto, and should not release the control of them in order that they might be subjected to process obtained by creditors of the company from a state court, nor should it award such creditors a priority of lien by reason of their proceeding in the state court.[1] The railroad property in this foreclosure suit was ordered by decree of the court to be sold on the ground that most of the lienholders were urging a sale, and it appeared that, in spite of the exercise of ability and great economy by a receiver during the three years he had had it under his management, no interest had been paid on any of the securities for a year, although the sale was opposed by one class of bondholders.[2] An announcement at a judicial sale of the property of an insolvent corporation, by the receiver, that the purchaser would also have the right, at his election, to take certain land, not covered by the order of sale, and acquired by the

[1] Farmers' Loan & Trust Co. *v.* San Diego Street Car Co., (1892) 49 Fed. Rep. 188.

[2] Bound *v.* South Carolina Ry. Co., (1892) 50 Fed. Rep. 853.

receiver during his administration of the corporate property, has been held not to render such sale invalid. Nor was the mere fact that the receiver. on taking possession, inventoried the property at a sum considerably greater than that fixed by the appraisers at a judicial sale of the property eight years afterwards, a ground for setting aside the sale for inadequacy of price.[1] The railway company, the property of which was by this decree in foreclosure suit to be sold, being situated entirely within the state of Kentucky, there were assignments of error to the United States Circuit Court of Appeals for the sixth circuit that allowing four months by the decree for redemption was erroneous; that the railroad should have been treated as "realty," and the time allowed for redemption should have been that prescribed in the Kentucky statute where judicial sales are had and mortgages are foreclosed upon real estate. The appellate court held that the time to be allowed for payment of a railroad mortgage after the entry of a foreclosure decree was within the discretion of the court, and the allowance of only four months in this case was not an abuse of the court's discretion. Further, that when railroad franchises and property, both real and personal, are mortgaged, and are to be sold on foreclosure, they were to be treated as an entirety, and this entirety was not "real estate" within the meaning of the Kentucky statute which requires an appraisement as a prerequisite to a judicial sale of real estate, and allows one year for redemption when the property does not bring two-thirds of its appraised value.[2] The sale of the property in this foreclosure

[1] Lake Superior Iron Co. *v.* Brown, Bonnell & Co., (1890) 44 Fed. Rep. 539.

[2] Columbia Finance & Trust Co. *v.* Kentucky Union Ry. Co., (1894) 60 Fed. Rep. 794. LURTON, Circuit Judge, said: "A like question was decided by the Supreme Court of the United States in Hammock *v.* Trust Co., 105 U. S. 77. The question in that case arose under the redemption statutes of the state of Illinois. The statute of that state provided for the redemption of lands 'sold under and by virtue of any decree of a court of equity for a sale of mortgaged lands.' It was provided, with reference to the latter case, 'that it should be lawful for the mortgagor of such lands, his executors, administrators or grantees, to redeem the same in the manner prescribed for the redemption of lands sold upon execution upon judgments issued at common law.' Upon elaborate consideration it was unanimously decided by that court that a railroad was not within the provision of that statute. The learned counsel for the appellant have undertaken to draw a distinction between the state of the law of Kentucky and that of Illinois, which they have argued is sufficient to distinguish this case from the case of Hammock *v.* Trust Co., *supra.* These

proceeding under the decree of the court was confirmed over the objection that it was sold at judicial sale as a whole, and not in the parcels in which it actually existed, and that either of such parcels was of sufficient value to discharge the lien for which the

distinctions are predicated upon the propositions: (1) That under the law of Illinois a railroad property consisted in (a) its franchises; (b) its movable property, such as rolling stock, supplies, etc., which were under the common law personalty; (c) its right of way, to which was affixed its rails, bridges, culverts, depots, etc., and which was clearly real estate. The conclusion drawn from this common-law division of its property was commented on by the Supreme Court of the United States as fatal to the insistence that when a railroad was mortgaged as an entirety it was redeemable as 'real estate,' within the meaning of the Illinois statutes conferring the right of redemption when real estate was sold to enforce the lien of a mortgage, which, under the law, covered the franchises, personalty and realty as unitedly constituting a railroad. In contrast it has been insisted that, under the decisions of the highest court of Kentucky, at the time the mortgage to the Central Trust Company was executed in 1888: (a) A railroad was a unit, and that its movable property was so affixed to its real estate as to be held fixtures, and, therefore, inseparable. To support this proposition the cases of Phillips *v.* Winslow, 18 B. Mon. 448, and Railroad Co. *v.* Elizabethtown, 12 Bush, 233, are cited. (b) That, in harmony with this, the same court has held that railroad shares descend as realty to the heirs, and are subject to dower. Price *v.* Price's Heirs, 6 Dana, 107, and Copeland *v.* Copeland, 7 Bush, 349. (c) That the franchises of a railroad company are not prerogative franchises, and that a railroad could be operated without a franchise. Railroad Co. *v.* Metcalfe, 4 Metc. (Ky.) 199. The cases cited do not, in our judgment, support the conclusions sought to be drawn. Phillips *v.* Winslow, *supra*, was a case where a trustee under second mortgage, made to secure an issue of bonds, and covering all the property of the company then in existence, as well as all after-acquired property, filed a bill to enjoin certain proceedings at law by judgment creditors, one of whom had levied on certain movable property and was about to sell, while the other had seized and sold, and bought at his own sale, under execution, certain cars, car wheels, firewood and stove coal, being supplies for the operation of the road. The levy was exclusively upon property acquired after the mortgage under which the plaintiff claimed, but was embraced in the clause covering after-acquired property. After deciding that the property was not subject to seizure by execution, because it was embraced in the mortgage, the court was confronted with the proposition that the plaintiff had an ample remedy at law by replevin or in an action for damages. This the court decided upon a consideration of the irreparable character of the damage to creditors having a mortgage upon a railway by a unit which would result to them from such a seizure in view of the unity of railroad property, and other great inconveniences resulting to the public from the interference with the equipment and necessary supplies of a common carrier. The court did not decide that the rolling stock of a railroad passed with the realty as a fixture. It certainly did not decide that cordwood and stove coal were fixtures,

whole was sold.[1] The court also considered the other objection to the confirmation of the sale, that other liens bore upon the same property of equal rank, and that the property ought to be resold, and for the benefit of all lienholders, as of no avail.[2] It is proper in a decree for sale on foreclosure proceedings against a railroad company upon a mortgage executed to secure its bondholders, the road being in the possession of a receiver, to direct that the sale be made subject to the standing obligations of the receiver, at the same time requiring the receiver to file a statement of his outstanding obligations in detail, so that the amount may be known with sufficient cer-

and yet the reasoning of the court was applied as much to such supplies as it was to the freight cars and detached car wheels, which were also in the levy. In the subsequent case of Railroad Co. *v.* Elizabethtown, *supra*, it was expressly ruled that a municipality could not dismember a railroad by a seizure for taxes of the engines and cars of a railway company. It is true that LINDSAY, C. J., did, in passing upon this question, observe that in Phillips *v.* Winslow, the engines and cars of a railroad 'were treated as fixtures.' But that case was not, as we have seen, put on any such ground, and indeed no such question arose for decision. Neither that case nor the decision in Railroad Co. *v.* Elizabethtown rested upon any technical consideration of the law of fixtures. The first went off, so far as the point now in question is concerned, upon the question of equitable remedy. The latter was vested [rested ?] upon the high and rational ground that a railroad was an entirety, and, being charged with *quasi* public duties as a common carrier, could not, from considerations of public policy, be disabled or dismembered by seizure under execution of its necessary equipments or supplies. It is true both cases recognized the unity of a railroad property resulting from its structure and utility. Severance of such a property is destructive of the interests of all concerned, and disables the road in the discharge of its public functions. Neither held that a railroad property considered as an entirety was technically realty."

[1] Central Trust Co. of New York *v.* Sheffield & Birmingham Coal, Iron & Ry. Co., (1894) 60 Fed. Rep. 9. PARDEE, Circuit Judge, said: "The answer to this objection is twofold: *First*, the decree so directed, and neither party complained until afterwards; *second*, there is no offer now by any one to pay a higher price for any parcel, or for the whole, than the sale realized, in case the bidding shall be reopened. * * * The decree is a sufficient answer, however, to the objection that the sale was not made in parcels. Hammock *v.* Trust Co., 105 U. S, 77–86; Central Trust Co. *v.* Wabash, etc., Ry. Co., 30 Fed. Rep. 332.

[2] Central Trust Co. of New York *v.* Sheffield & Birmingham Coal, Iron & Ry. Co., (1894) 60 Fed. Rep. 9. The circuit judge said: "The record of the cases discloses that there are other and large liens on the property of equal and perhaps prior rank to the intervener's lien. This, in part, accounts for the price brought at the sale, as the purchaser, as well as other bidders, knew that the property offered was incumbered. But such fact is no reason why the sale, as made, should not

tainty to enable intending purchasers to bid with confidence.[1] The United States Circuit Court of Appeals for the fourth circuit has declared the following rules in a foreclosure proceeding participated in by different lienholders: The owner of second consolidated railroad mortgage bonds filed a foreclosure bill, and, according to the prayer of his bill, the court appointed a receiver and required all lienholders to come into the cause, and enjoined them from asserting their claims in any other case. Cross-bills were filed by all the lien claimants, including the holders of prior and subsequent mortgage bonds. These cross-bills asked affirmative relief and the sale of the property. For nearly three years the Circuit Court treated the suit as a consolidated case, and finally decreed a sale free of all liens. It was held by the Court of Appeals that it was too late for any party to object to the decree, that it was not in conformity to the prayer of he original bill, or to contend that because the lienors had filed cross-bills, instead of obtaining leave to file original bills, the pleadings were irregular.[2] A court of equity, pending an appeal, without supersedeas, from a final decree in a foreclosure suit, settling the priority of liens and fixing a day for sale, has power to postpone the order if a sale on the day fixed would be oppressive or unjust. And such a postponement should be made in such a suit to foreclose a matured mortgage, when an appeal has been taken from the decree of sale, the result of which might be disastrous to the purchaser, or where the sale, if incapable of being rescinded, would render nugatory a decision in favor of appellants.[3] In proceedings to foreclose the liens of the state of South Carolina on railway property as the guarantor of the railway bonds, as also the mortgages on the same property, the United States Circuit Court for that district refused to authorize the sale of land, free from such liens, at private sale, not being fully informed as to its selling value. In the opinion of the court, on foreclosure proceedings, where a receiver has been appointed, but the relative rights of the various parties had not been established, the fact that the mortgages authorized the sale of lands

be confirmed, the other lienholders not complaining, and otherwise being able tc take care of themselves."

[1] Bound *v.* South Carolina Ry. Co., (1893) 58 Fed. Rep. 473.

[2] Ibid.

[3] Bound *v.* South Carolina Ry. Co., (1893) 55 Fed. Rep. 186.

not needed for corporate purposes, and the application of the proceeds by the trustees to the extinguishment of the oldest liens, would not justify such sale by the court, in the absence of consent by all the parties, and the mere absence of counsel from the hearing of a motion for the purpose of ordering such a sale would not amount to consent.[1] It is proper to order a sale of the property mortgaged, where shown to be in the best interests of all concerned, notwithstanding objections of a minority of the bondholders, when apparent that controverted questions of priorities and validity of some of the bonds can be afterwards settled.[2] The decree for sale of railroad property in foreclosure proceedings should name an upset price sufficiently large to cover claims against the proceeds of the sale.[3]

§ 540. **Purchasers at sales under the decrees — their rights and liabilities.**— Where a railroad has been in the hands of a receiver appointed by the United States Circuit Court, is sold, and the purchaser, as part of the consideration, covenants to discharge all existing debts and liabilities of the receivership, it is the duty of such court to protect the purchaser against all demands which are not just and proper demands against the receiver, and to that end to require all such demands to be presented to the court for allowance. And where, on the strength of such a covenant, a person brings an action in the state court against the purchaser to recover for a tort to his realty committed by the

[1] Bound *v.* South Carolina Ry. Co. (Mayfield, Intervener), (1891) 46 Fed. Rep. 315. See Kneeland *v.* Trust Co., 136 U. S. 89; s. c., 10 Sup. Ct. Rep. 950.

[2] First National Bank of Cleveland *v.* Shedd, 121 U. S. 74; s. c., 7 Sup. Ct. Rep. 807.

[3] Blair *v.* St. Louis, Hannibal, etc., R. R. Co., 25 Fed. Rep. 232. See, also, McIlhenny *v.* Binz, (Tex.) 13 S. W. Rep. 655. When a petition for an interlocutory decree of sale of railway property should be denied, see Pennsylvania R. Co. *v.* Alleghany Valley R. Co., 42 Fed. Rep. 82. When a court will not hear a motion in behalf of an individual bondholder to set aside a foreclosure sale under its decree, see Meyer *v.* Utah & Pleasant Valley R. R. Co., 3 Utah, 280. When an order of the sale of securities adjudged to be subject to the lien of a mortgage with the mortgaged property is conclusive, see Herring *v.* New York, Lake Erie, etc., R. R. Co., 105 N. Y. 340. When an order for sale of insolvent corporation's property granted to a receiver will not be vacated by the court, see Farmers' Co-operative Mfg. Co. *v.* Drake, (Ga. 1895) 22 S. E. Rep. 1004. What will be required to justify a reopening of the foreclosure proceedings where a sale has been decreed, see Leavenworth County *v.* Chicago, Rock Island, etc., Ry. Co., 25 Fed. Rep. 219. See, also, Robinson *v.* Iron Railway Co., 135 U. S. 522; s. c., 10 Sup. Ct. Rep. 907.

receiver, such demand being primarily chargeable on the fund in the federal court, arising from the sale of the railroad property, the federal court should restrain the prosecution of the action, and require the plaintiff to present his claim to it, inasmuch as a judgment on such a claim in the state court would entitle the plaintiff to satisfy it out of any property in the hands of the purchaser subject to levy; and the purchaser's appearance in the state court would not be a waiver of its rights to have the proceedings in the state court restrained, where the nature of the suit did not once appear, but it invoked the jurisdiction of the federal court as soon as its right to do so was revealed by the pleadings.[1] The federal court, in which, under foreclosure of a railroad mortgage there had been a sale, directed its receiver to turn over the possession of the road to another railroad company, the assignee of the purchaser at the sale, the court reserving the right to resume the possession if the assignee should thereafter refuse to pay into court any part of the purchase price. It was held, on an application of the assignee for a writ of assistance, that the order of the court just returned brought the assignee within Equity Rule 10, which provides that every person not a party to a cause, in whose favor an order has been made, shall be enabled to enforce obedience to such order by the same process as if he were a party to the same, and that a writ of assistance would issue in favor of such assignee against another railroad company which unlawfully refused to surrender possession of a part of the road.[2] It is a well-established principle that the mere purchase of a railway under a foreclosure sale by a new corporation does not of itself make such new corporation liable for the obligations of the old one.[3] In a case before the United States Supreme Court it appeared that a railroad company, which had purchased the property and franchises of a railroad company against which a mortgage had been foreclosed, neither renounced the contract under which the insolvent company had used the land constituting its approaches to a ferry belonging to a ferry company which by a contract with covenants on the part of the insolvent railroad company to use solely its ferry for the purposes of transportation of freight and passengers

[1] Jesup *v.* Wabash, St. L. & P. Ry. Co., (1890) 44 Fed. Rep. 663.

[2] Farmers' Loan & Trust Co. of New York *v.* Chicago & Atlantic Ry. Co., (1890) 44 Fed. Rep. 653.

[3] Stewart's Appeal, 72 Pa. St. 291; Vilas *v.* Milwaukee, etc., Railway, 17 Wis. 497; Smith *v.* Chicago & Northwestern Railway, 18 Wis. 17.

across this navigable stream, nor made any further arrangement with the ferry company after it became the purchaser. It maintained, however, possession of the land. The purchasing company becoming insolvent, and the mortgage it had executed being in the process of foreclosure, and the property in the hands of a receiver, the ferry company intervened and set up a claim on the theory mainly of the relation of landlord and tenant, for the use of its land, including, also, breaches of certain covenants as to using its ferry alone and not directing any of the traffic to other lines, as it charged had been done. The court regarded the theory of the intervention as a serious obstacle in the way of doing substantial justice between the parties, but recognized the right of the ferry company to equitable relief as against the purchasing company, as then represented by the receiver, and remanded the case to the Circuit Court for a change of pleadings and such further proceedings as might be consonant with justice and in conformity to its opinion.[1] A purchaser of a railroad at a foreclosure sale, who had no direct agency in the act complained of, will not ordinarily be liable for an act of the receivers operating the road prior to the sale; but if the act of the receivers created a nuisance, which was in existence at the time of the purchase, and the purchaser then had notice of the acts constituting the nuisance, and continued the nuisance afterwards, and in consequence thereof plaintiff's land was overflowed, rendered untillable, and his crops ruined, the Missouri Appellate Court held the purchaser to be liable.[2] They further held that written notice of the existence of a nuisance served upon the chief engineer of the former railway company could not import notice to a corporation (not then in existence) that subsequently purchased the railway at foreclosure sale; but where such officer was retained in the service of the receivers, and while so retained acquired full knowledge of all the facts constituting the nuisance, and the continuation thereof, and was continued in the office in the service of the subsequent purchaser, under such conditions as necessarily gave rise to the inference that such knowledge remained fixed in his memory when his employment by the purchaser began, then his knowledge must be deemed the knowledge of the purchaser. A purchaser at a foreclosure sale having been allowed in the

[1] Wiggins Ferry Co. *v.* Ohio & Mississippi Ry. Co., (1892) 142 U. S. 396.

[2] George *v.* Wabash Western Ry. Co., (1890) 40 Mo. App. 433.

decree confirming the sale a credit by reason of a certain receipt filed by him, the United States Circuit Court of Appeals for the fifth circuit held that it was error to reject such credit in the subsequent decree distributing the proceeds of sale.[1] The purchaser of this railroad property on foreclosure was entitled to a credit for taxes paid by it where the taxes were a lien upon the property, the date of the assessment not appearing, that being the date when the lien attaches under the statutes of Florida. The United States Circuit Court of Appeals for the fifth circuit held that it could not be said that the refusal to allow such a credit was error.[2] There being a provision in a railroad foreclosure decree that certain specified classes of claims constituted a lien prior to that of the mortgage bonds and a direction that the sale should be made subject to such lien, the purchaser at the sale would be estopped from objecting to the payment of a claim which belonged to one of the classes specified.[3] The mortgagor railroad company here, pending the foreclosure of a mortgage upon its property, etc., leased to another railroad company an equal right to the use of a designated part of the road for a period of twenty years. The foreclosure decree provided that the purchaser at the sale should be at liberty to abandon or disclaim any leasehold interest or contracts or other agreements entered into by the mortgagor after the commencement of foreclosure proceedings. The lessee railroad company declined to surrender the use it had acquired under this agreement with the mortgagor company to the assignee of the purchaser at the foreclosure sale upon various pretexts. The assignee applying to the court for a writ of assistance to enable it to secure the exclusive use of this part of the road purchased, it was held that the purchaser's right to abandon and disclaim the lease, as provided in the decree of sale, was not affected by the receipt of the rent by the receiver during the pendency of the foreclosure proceedings and his acquiescence in the lease, and that all right of possession in the lessee ceased on being notified of the purchaser's intention to disclaim and abandon. It appeared also that just after the foreclosure sale the assignee of the purchaser notified the lessee of its intention to disclaim the lease, and forbade the latter from using

[1] Cutting *v.* Tavares, O. & A. R. Co. (Florida Central & P. R. Co., Intervener), (1894) 61 Fed. Rep. 150.

[2] Ibid.

[3] St. Louis S. W. Ry. Co. *v.* Stark, (1893) 55 Fed. Rep. 758.

the road at the expiration of thirty days from the date of the notice. It was held by the court, upon the special contention of the lessee, that the receipt of the rent for those thirty days by the assignee of the purchaser, which was expressly stated to be without prejudice to its rights to abandon the lease, was not such a consent to the lessee's possession as to constitute it a tenant from year to year within the meaning of the Indiana Statutes, which provide that all general tenancies where premises are occupied with the consent, either express or constructive, of the landlord, shall be deemed tenancies from year to year, to be determined by three months' notice to be given the tenant before the expiration of the year.[1] Lands of a railroad company had been leased to one who built upon them warehouses, etc. There were provisions in the leases for the purchase of these improvements by the lessor or their removal by the lessee at the end of the term. These leases were made subsequent to the execution of mortgages by the railroad company and subject to them. In a bill filed by the final successor to the purchaser at foreclosure sale under the mortgages against the assignees of these leases to declare them void, a contention of the defendants was that the failure of the mortgagor to bring them in as parties defendant to the foreclosure suit operated as a recognition of their status as tenants and a ratification of their leases. The court held against this contention as the lessees were not necessary parties to that suit, and so far as the mortgagor was concerned, the rights of these lessees were extinguished by the foreclosure sale.[2]

§ 541. Who may be heard on petition in foreclosure suits.— Persons who are not parties to a suit cannot, in general,

[1] Farmers' Loan & Trust Co. of New York *v.* Chicago & Atlantic Ry. Co., (1890) 44 Fed. Rep. 653. And the undisputed facts showing that the purchaser, after the foreclosure sale, never waived its right to abandon and disclaim the lease, the federal court in which the mortgage was foreclosed, in the exercise of its primary jurisdiction over the matter, determined to issue a writ of assistance in favor of the purchaser, notwithstanding the issuance of a temporary injunction by the state court in which the purchaser appeared, restraining it from interfering with the lessee's possession, should the lessee continue to hold the property.

[2] Tyler *v.* Hamilton, (1894) 62 Fed. Rep 187. As to what passes by a sale under foreclosure of the property of the corporation, see Lawrence *v.* Morgan's La. & Tex. R. & Steamship Co., 39 La. Ann. 427; s. c., 2 So. Rep. 69; Dow *v.* Beidleman, (Ark.) 5 S. W. Rep. 297; Washington, Ohio & W. R. Co. *v.* Lewis, (Va.) 2 S. E. Rep. 746.

file a petition therein for any cause; but persons belonging to a class represented in the suit, such as mortgage creditors represented by the trustees of the mortgage, are regarded as *quasi* parties, and may be heard on petition or motion.[1] In suits brought by a trustee for foreclosure, or otherwise affecting trust property, the beneficiaries of the trust will frequently be allowed to intervene for the purpose of protecting their interest.[2] A petition seeking to recover damages from the trustee for maladministration of the trust cannot be filed as a cross-bill in a proceeding for the foreclosure of a deed of trust. The matter set up in such a bill is not necessary as a defense to the original bill, but would be matter entirely foreign to the primary object of the bill and would make it an original, independent bill.[3] In a foreclosure suit against a railroad company another railroad company intervened and petitioned the court to allow a claim which it made under certain traffic contracts entered into between several railroad companies. The petition was dismissed in the United States Circuit Court. The intervener appealed to the United States Circuit Court of Appeals for the eighth circuit and the appellate court affirmed the decree of the court below. It was held that such an agreement between railroad companies, by the terms of which all their roads were to be operated as to through traffic as if "operated by one corporation which owned all of them," and which provided for an actual division of such traffic, and, where this was not done, for a division of the gross earnings thereof, the obvious purpose of the agreement being to suppress or limit competition, and to establish rates without regard to their reasonableness, was contrary to public policy and void.[4] The appellate court further held in this case that one

[1] Fidelity Trust & Safety Vault Co. *v.* Mobile Street Ry. Co., (1893) 53 Fed. Rep. 850 (a bill to foreclose a mortgage). Citing Anderson *v.* Railroad Co., 2 Woods, 628.

[2] Fidelity Trust & Safety Vault Co. *v.* Mobile Street Ry. Co., (1893) 53 Fed. Rep. 850; citing Fost. Fed. Pr. 291; Carter *v.* City of New Orleans, 19 Fed. Rep. 659.

[3] Fidelity Trust & Safety Vault Co. *v.* Mobile Street Ry. Co., (1893) 53 Fed. Rep. 850.

[4] Chicago, M. & St. P. Ry. Co. *v.* Wabash, St. L. & P. Ry. Co., (1894) 61 Fed. Rep. 993. CALDWELL, Circuit Judge, said: "A railroad company is a *quasi* public corporation and owes certain duties to the public, among which are the duties to afford reasonable facilities for the transportation of persons and property and to charge only reasonable rates for such service. Any contract by which it disables itself from performing these duties, or which makes it to its interest not to perform, them or removes all incentive to their performance, is contrary to public policy and void." The court cited in support of its ruling Railroad

party to such illegal agreement, claiming to have performed its part of the same, could not maintain a suit to enforce division of earnings by another party thereto, the traffic not having been divided.[1] In this intervention in a foreclosure suit it was held not

Co. *v.* Closser, 126 Ind. 348; s. c., 26 N. E. Rep. 159; Gulf, C. & S. F. R. Co. *v.* State, (Tex.) 10 S. W. Rep. 81; State *v.* Standard Oil Co., (Ohio) 30 N. E. Rep. 279; Texas & P. Ry. Co. *v.* Southern Pac. Ry. Co., (La.) 6 So. Rep. 888; Gibbs *v.* Gas Co., 130 U. S. 396; s. c., 9 Sup. Ct. Rep. 553; Morris Run Coal Co. *v.* Barclay Coal Co., 68 Pa. St. 173; Salt Co. *v.* Guthrie, 35 Ohio St. 666; Stanton *v.* Allen, 5 Denio, 434; Hooker *v.* Vandewater, 4 Denio, 349; Chicago Gaslight & Coke Co. *v.* People's Gaslight & Coke Co., 121 Ill. 530; s. c., 13 N. E. Rep. 169; West Virginia Transp. Co. *v.* Ohio River Pipe Line Co., 22 W. Va. 600; W. U. Telegraph Co. *v.* American Union Tel. Co., 65 Ga. 160; Sayre *v.* Association, 1 Duv. 143; U. S. *v.* Trans-Missouri Freight Assn., 58 Fed. Rep. 58; s. c., 7 C. C. A. 15.

[1] Chicago, M. & St. P. Ry. Co. *v.* Wabash, St. L. & P. Ry. Co., (1894) 61 Fed. Rep. 993. CALDWELL, Circuit Judge, said: "The illegal and void contract has not been executed, and the appellant invokes the aid of the court to compel the Wabash Company to execute it on its part by pooling its earnings. It may be conceded that the illegal contract has been performed on the part of the appellant, though it does not appear to have done anything more than to sign the contract. The only thing it could do towards a performance of the contract was not to compete for the business. This was a violation of its duty to the public, and illegal. But a contract performed on one side only is not an executed contract. Where an illegal act is to be done and paid for, the contract is not executed until the act is done and paid for. A court will not compel the act to be done, even though it has been paid for. Neither will it compel payment, although the act has been done, for this would be to enforce the illegal contract. The illegality taints the entire contract, and neither of the parties to it can successfully make it the foundation of an action in a court of justice. The Wabash Company performed the service that earned the money the appellant is seeking to recover. The appellant earned no part of it. There is nothing in the record to show that the appellant would have carried more or the Wabash Company less freight if the contract had never been entered into. The money demanded was received by the Wabash Company for freight tendered to it by shippers themselves and carried by it over its own line. It was legally bound to accept the freight thus tendered, and was entitled to receive the compensation for the carriage, and cannot be compelled to pay the money they earned or any part of it to the appellant on this illegal and void contract. * * * Courts will not lend their aid to enforce the performance of a contract which is contrary to public policy or the law of the land, but will leave the parties in the plight their own illegal action has placed them. Central Transp. Co. *v.* Pullman's Palace Car Co., 139 U. S. 24; s. c., 11 Sup. Ct. Rep. 478; Gibbs *v.* Gas Co., 130 U. S. 396; s. c., 9 Sup. Ct. Rep. 553; Texas & P. Ry. Co. *v.* Southern Pac. Ry. Co., 41 La. Ann. 970; s. c., 6 So. Rep. 888; Morris Run Coal Co. *v.* Barclay Coal Co., 68 Pa. St. 173; Hooker *v.* Vandewater, 4 Denio, 349."

to be necessary, under the Missouri statute which gives a mechanic's lien for materials furnished to a railroad company, to show that the materials were incorporated in the construction of the road. Further, that the railroad, being in the hands of a receiver appointed by the court, he alone was a necessary defendant in an action to foreclose such a mechanic's lien under the statute which provides that any person or corporation "owning or operating" the railroad shall be made a party to such proceedings.[1]

§ 542. **Disposition in decree of proceeds of sale.**— The federal court for the eastern district of Missouri had under a judgment creditor's bill appointed a receiver and ordered the property of a railroad company sold. The property was sold subject to the lien of a mortgage covering its franchises, etc., to secure bonds and "to all liens for taxes." As to the distribution of the proceeds of the sale the court, inasmuch as the receiver had been in the possession of the property during the time when a levy might be made upon it for taxes on the personalty, ordered the payment of the taxes on personal property out of the proceeds of the sale in preference to all other claims; but as the state had a permanent lien for taxes on realty and the sale was subject thereto, did not order those taxes to be paid out of the proceeds. It was ruled further that the proceeds of the sale of the property being insufficient to pay the judgment creditors, and there having previously been no application to the payment of judgment creditors

The court disapproved Central Trust Co. *v.* Ohio Cent. R. Co., 23 Fed. Rep. 306, as not supported by authority and unsound in principle.

[1] Central Trust Co. of New York *v.* Chicago, K. & T. Ry. Co. (Holton-Warren Lumber Co., Intervener), (1893) 54 Fed. Rep. 598. PHILIPS, D. J., said: "Where, on petition of creditors, a court of chancery takes possession of a railroad, and appoints receivers to run and operate it, the property passes in *custodia legis*, and the receivers become the representatives of the corporation for the very purpose of protecting and preserving the property for the benefit of both creditors and stockholders. While the corporation, as a legal entity, is not disturbed, and its board of directors still exist, with power to guard and preserve the franchise, and would resume jurisdiction in management upon the surrender of the property by the court, yet they do not operate and control it while so in court, and I think the evident purpose of the statute * * * was to prevent the enforcement of such liens against the *corpus* of the corporation simply *in rem.* It seeks to have the railroad represented in court." When the petition of an intervening creditor should be dismissed, see Penn *v.* Calhoun, 121 U. S. 251.

of any of the railroad company's property which should have been applied to the payment of open accounts, the holders of such accounts were not entitled to participate in the proceeds of the sale. As to intervening judgment creditors, the rule was declared to be that the bill to reach the property which could not be effectively reached at law being filed by certain judgment creditors for the benefit of all judgment creditors of the insolvent railroad company, and no order having been made requiring others to intervene by a certain time or be barred of their rights, all judgment creditors who chose to intervene were entitled to share ratably with complainants in the proceeds of the sale of the property, even though some did not intervene until after the interlocutory decree ordering the sale; and the right of these subsequent interveners to share ratably was not affected by the fact that the bill prayed that after a sale the proceeds should be distributed among the persons in whose behalf the suit was brought "according to their respective rights and equities," as the original complainants and prior interveners had no prior lien on all the property sold when the bill was filed.[1] The decree of foreclosure in this case having provided, in accordance with the terms of the mortgage, that the purchase money should be applied "first to the payment in full, if it be sufficient, or, if not, to the payment *pro rata* of all defaulted coupons," the United States Circuit Court of Appeals for the fifth circuit held that a decree of distribution of the proceeds of the sale which directed a *pro rata* payment on the bonds themselves, before paying the interest coupons due, was erroneous.[2] A bill in equity to foreclose a railroad mortgage for non-payment of overdue interest, the principal being payable at a future day, was here taken *pro confesso*, the company appearing, but not answering. Under the decree of the court a sale was made, and, it appearing that there was a surplus over and above what was necessary to pay the overdue interest, costs and expenses, it was ordered by the court that this surplus be applied to the reduction of the principal sum due upon the bonds, and a decree entered that the balance of such principal sum remaining after the application of this surplus was due and payable from the company to the holders of the bonds, and that

[1] George *v.* St. Louis Cable & Western Ry. Co., (1890) 44 Fed. Rep. 117.

[2] Cutting *v.* Tavares, O. & A. R. Co. (Florida Cent. & P. R. Co., Intervener), (1894) 61 Fed. Rep. 150.

the trustee recover it for them, with interest until paid. The Supreme Court of the United States held that the application of this surplus was properly made, but the decree declaring the remainder of the principal due and immediately payable was irregular and was not warranted by the pleadings.[1] They declared in the same case these rules as to pleadings and appeals in such foreclosure suits: The defendant in a bill in equity, taken *pro confesso*, is not precluded from contesting the sufficiency of the bill or from insisting that the averments in it do not justify the decree. A decree on a bill taken *pro confesso* may be attacked on appeal, if not confined to the matter of the bill. The ninety-second rule in equity does not authorize a decree to be entered in a suit in equity for the foreclosure of a mortgage for a balance due to the complainant over and above the proceeds of the sale, if, as a matter of fact, such balance has not become payable. A railroad company, the road, property and franchises of which have been sold under a decree for the foreclosure of a mortgage entered on a bill taken *pro confesso*, may prosecute an appeal from the final decree distributing the proceeds of the sale and adjudging a balance still due the mortgage creditors.[2] This rule has been declared in the United States Circuit Court of Appeals for the eighth circuit: That the Circuit Court of Appeals cannot take knowledge, actual or judicial, of what may appear upon the records of the District and Circuit Courts within the boundaries of the judicial circuit, and to support the rights of appeal cannot assume the existence of necessary facts which do not appear of record in such courts. And upon an appeal from an allowance of a claim in railway mortgage foreclosure proceedings by one styling himself "the purchasing trustee of defendant's property," where it did not appear from the record that the property had been sold under the decree, or what interest or right appellant had in the proceedings, for whom he was trustee, or that the moneys out of which the claim was paid were a part of any fund in which he had an interest, the court held that the appeal should be dismissed, appellant not showing by the record any right to appeal.[3]

[1] Ohio Central R. R. Co. *v.* Central Trust Co. of New York, (1890) 133 U. S. 83.

[2] Ibid.

[3] Fitzgerald *v.* Evans, (1892) 49 Fed. Rep. 426. SHIRAS, J., speaking for the court, took occasion to say: "In view of the action we have felt com-

§ 543. **Allowances in foreclosure suits.**—Where there had been a foreclosure of a mortgage executed by a corporation for $145,000, and interest, a decree entered on default, and the property bought in by one of the bondholders for less than the mortgage debt, an allowance was made to the mortgagee, a trust company, of $1,000, and $500 allowed to its counsel. Upon exceptions to the master's report in this matter of allowances, it was held that no further allowance to the trustee for services or

pelled to take in this matter, we deem it advisable to call attention to the practice that should be followed in cases of railroad foreclosures, where a sale of the property is had before the rights of all intervening parties are determined, and where, by the terms of the decree, the court reserves full power to hear such matters after the sale, with the right to subject the property and its proceeds to the payment of claims finally adjudged to be prior to the lien of the mortgage. When a sale is made under a decree of the kind described, it is the duty of the purchaser, upon a confirmation of the sale, to make himself a party to the foreclosure proceedings by filing therein a supplemental bill or petition of intervention, setting forth the fact that he has, by purchase of the property, become a party in interest, thus showing that he has become subject to the burdens and entitled to the benefits of the decree under which he has purchased the property. Furthermore, if the purchaser does not reside within the territorial limits of the jurisdiction of the court, he should appear by an attorney who is a member of the bar of the court having charge of the foreclosure proceedings, so that when need arises the court may be enabled to have before it all persons interested in resisting the allowance or payment of claims which are asserted to be entitled to priority of payment. It not unfrequently happens that the purchasers at railway foreclosure sales may reside at distant points and without the jurisdiction of the court. If the purchaser who thus resides at a distance does not become a party to the record, and have an attorney representing him upon whom service may be made, the court and litigants are put to a great disadvantage in disposing of the claims asserted against the property or its proceeds. Many of the claims are of small amounts, and if, before the same can be allowed and paid, it is necessary to procure orders for service upon a purchaser living in New York or some other distant point, and to complete such service at his place of residence, the expense thereof will eat up the claim. It is due to the court and necessary for the prompt and inexpensive disposition of claims of the nature indicated, that the purchaser shall become a party to the record and subject himself to the jurisdiction of the court in the manner indicated. If the purchaser fails in this particular, then the court having jurisdiction of the foreclosure proceedings should, by appropriate action, compel the purchaser to become a party to the record in order that the business of winding up the foreclosure case and finally settling the rights of all interested may be proceeded with in an orderly way. If a purchaser at a foreclosure sale makes himself a party to the record in the manner indicated then it will be the duty of the Circuit Court to cause notice to be given him before passing upon inter-

counsel fees was warranted by the facts of the case.[1] It appeared here that on maturity of bonds secured by a railroad mortgage, after most of them had been returned and the holders of nearly all of the bonds outstanding had agreed to an extension of time, the trustee of the mortgage, on his motion, and without request by the bondholders, brought suit to foreclose. The suit was never prosecuted to a decree, proceedings on a second mortgage being afterward instituted in the federal court. Upon the petition by this trustee for allowances in the bondholder's suit to foreclose the second mortgage, SIMONTON, Circuit Judge, held that the suit by him was unnecessary and declined to allow him compensation or counsel fees. The lien of the first mortgage was not questioned in the foreclosure proceedings on the second mortgage; the holders of the bonds secured by the first mortgage had consented to an extension of time. The court held that the duty of the trustee, under the first mortgage, was to see that the amount due thereunder was determined, and a decree made concerning the interests of the bondholders; and for anything more than the performance of that duty he should not be allowed compensation

vening claims or directing their payment from the fund in court, and thus full opportunity will be afforded to all parties in interest to be heard for the protection of their rights." As to rules of distribution of proceeds of a foreclosure sale, see Pinkard *v.* Allen, 75 Ala 73. As to the rule of distribution of the proceeds of a sale where there is to be a distribution between bondholders secured by first and second mortgages, see Morton *v.* New Orleans & Selma Ry. Co., 79 Ala. 590. Rules as to the application of proceeds of sale to bonds purchased under an agreement of the company not to issue any more of that series. McMurray *v.* Moran, 134 U. S. 150; s. c., 10 Sup. Ct. Rep. 427.

[1] Boston Safe Deposit & Trust Co. *v.* Adrian, Mich., Water Works, (1891) 47 Fed. Rep. 8. SWAN, J., thus spoke of the principles governing such allowances: "While it is well settled that a trust fund is chargeable with the expenses of its own administration, and that counsel fees may be properly taxed against such a fund, the present is not a case calling for the application of that rule. Such allowances are frequently and properly made in cases where the trust fund had been rescued from waste or destruction arising from the fraud, neglect or misconduct of trustees, or when the energy and efforts of creditors or others interested have saved the property for those entitled. It is also true that a creditor primarily seeking satisfaction of his own debt, who has realized, by his diligence and at his own expense, a fund available for the benefit of others as well as himself, is entitled to reimbursement of his costs and expenses, either out of the fund or by a proportional contribution from those who accept the benefit of his efforts. The cases of Trustees *v.* Greenough, 105 U. S. 527; Railroad Co. *v.* Pettus, 113 U. S. 116; s. c., 5 Sup. Ct. Rep. 387; Hobbs *v.* McLean, 117 U. S. 567; s. c., 6 Sup. Ct. Rep. 870, afford examples of

or counsel fees.[1] As to allowances on foreclosure suits it was ruled in this case that an order might be made on the receivers for the payment of expenses incurred by a mortgagee in a suit of foreclosure, where the mortgage made provision for such expenses. But where the mortgaged property was insufficient to pay the mortgages, an order could not be made for allowance of counsel fees of the mortgagee to be paid out of money in the hands of the receivers.[2] The United States Circuit Court of Appeals for the fifth circuit has held, in the suit of a stockholder, in behalf of itself and other stockholders, should they come in, against a railway corporation, alleging the making of an illegal and void contract by the corporation, and praying for an account, an injunction, and the appointment of a receiver, an allowance for compensation to the complainant for solicitor's fees, pending an appeal from an order appointing a receiver and continuing a restraining order, to be premature.[3] In an action by the holder of second mortgage bonds of a railroad company for the appointment of a receiver, and a receiver was, therefore, appointed with the consent of all interested parties, and to the advantage of all, it was held that the services rendered by complainant's attorneys, being for the common benefit, should be paid for from the assets of the company.[4] This foreclosure suit was brought by a bondholder, who in his bill alleged *laches* on the part of the trustees of the mortgage, and made them, and all prior lienholders, parties. These prior lienholders, by cross-bills, also prayed foreclosure of their own liens, so that, as a result of the litigation, the property was decreed to be sold free of all liens. Upon a ques-

the propriety of their allowances. In those cases costs and expenses were allowed the successful plaintiffs for the recovery of salvage of an imperiled fund, which, but for the diligence and activity of the creditor or trustee, would have been wholly lost to the beneficiaries or seriously depleted. They are marked, too, by the fact that success was only attained by long and laborious effort, and at great expense, against fraud, neglect, misconduct or vigorously contested hostile claims. It is just and equitable that such meritorious service should be adequately compensated by the parties benefited. No such features characterize this case." See, also, Williams *v.* Morgan, 111 U. S. 699; s. c., 4 Sup. Ct. Rep. 638.

[1] Bound *v.* South Carolina R. Co.; Ex parte Walker; Ex parte Calder, (1894) 62 Fed. Rep. 536.

[2] Mercantile Trust Co. *v.* Missouri, K. & T. Ry. Co., (1889) 41 Fed. Rep. 8.

[3] Jacksonville, T. & K. W. R. Co. *v.* American Construction Co., (1893) 57 Fed. Rep. 66.

[4] Bound *v.* South Carolina Ry. Co., (1890) 43 Fed. Rep. 404, ordering a

tion of allowance of counsel fees, the federal court, by which the sale was decreed, held that the trustees of the various mortgages must be considered as acting in the interest of their own bondholders alone; and that the counsel fees of the various parties should not be charged upon the fund as a whole, but upon that part of the proceeds appropriated to the payment of the mortgages respectively. The court made this exception, and held that where part of the bondholders under a mortgage dissented from the action of their trustees in declaring the mortgage due for default in interest, and contested the matter in the foreclosure proceedings, such dissenting bondholders must pay their own counsel fees.[1] Certain bondholders appeared by their counsel, and contested the creditors' rights in a suit by bondholders to foreclose a mortgage of the corporate property and franchises, and took various steps during the progress of the case involving labor and responsibility on their counsel; subsequently, during the progress of the litigation, these contesting bondholders sold their bonds. On petition by their counsel to be allowed a fee payable out of the dividend which would go to these bondholders, it was held that the counsel had a lien upon such dividend, and that the purchaser of the bonds *pendente lite* took subject to this lien.[2] In a case where the complainant in a bill for the foreclosure of a railroad mortgage was the holder of a majority of the bonds secured by the mortgage, and the trustee, by agreement with the complainant, had declined to act in the foreclosure proceedings, and was made a co-defendant, full allowance having been made to the counsel of complainant and to the receiver for his services, all for duties which by the mortgage were assigned to the trustee, the United States Circuit Court held that it was not error to refuse an allowance also to trustee's counsel.[3]

payment to the attorneys on account as was done in Central Trust Co. *v.* Wabash, etc., Ry. Co., 23 Fed. Rep. 675.

[1] Bound *v.* South Carolina Ry. Co., (1894) 59 Fed. Rep. 509.

[2] Mahone *v.* Southern Tel. Co., (1887) 33 Fed. Rep. 702.

[3] Investment Co. of Philadelphia *v.* Ohio & Northwestern R. R. Co., (1891) 46 Fed. Rep. 696.

CHAPTER XXIX.

RECEIVERS IN FORECLOSURE SUITS.

§ 544. Receivers—their appointment — when they should be appointed — who may be appointed — their discharge and removal.

545. Conditions attached to the appointment of a receiver.

546. Receiver's right as to possession of the property of the insolvent corporation.

547. The relation of the receiver to property leased by the corporation coming into his hands.

548. Powers of receivers as to contracts, etc.

549. Power of the court and its receivers as to regulating wages of employees.

550. Receiver's certificates — when they will be authorized — the lien of such certificates and its enforcement.

§ 551. Rules as to claims against receiver growing out of rolling stock coming into his possession.

552. Application of earnings of the road during receivership.

553. Jurisdiction of actions against receivers.

554. Claims against receivers for injuries to persons or property during receivership.

555. Rules as to actions for injuries to persons during receivership.

556. Rules as to allowances to receivers for counsel and expenses of parties in actions where receivers are appointed — what will be allowed and what not.

557. Actions allowed a receiver for the protection and benefit of the property in his hands.

§ 544. Receivers — their appointment — when they should be appointed — who may be appointed — their discharge and removal.— The appointment of a receiver has been held to be justified where it appeared that a railroad, heavily mortgaged, had made several defaults in the payment of interest, aggregating over $1,000,000; that the business was decreasing, with probability of further decrease from competition with new lines; that it was in need of repairs and improvements; that the bondholders were not in harmony; that a foreclosure was about to be decreed; and that no other way existed for applying the rents and profits of the road to its debts.[1] It appeared in this action, upon the foreclosure of a railroad mortgage and the appointment of a receiver, that the allegations of the bill and answer were in conflict as to the solvency of the company, the

[1] Mercantile Trust Co. *v.* Missouri, K. & T. Ry. Co., (1889) 36 Fed. Rep. 221. See Railroad Co. *v.* Cowdrey, 11 Wall. 463; Gilman *v.* Telegraph Co., 91 U. S. 603; Dow *v.* Railway Co., 124 U. S. 652; s. c., 8 Sup. Ct. Rep. 673; Kountze *v.* Hotel Co., 107 U. S. 378; s. c., 2 Sup. Ct. Rep. 911.

condition and care of its property, and the wisdom and economy of its methods of operation; but as it also appeared that a majority of the stock of the railroad company was in the hands of a construction company, with substantially the same officers as the railroad company, the officers of which construction company were adverse to those of the mortgage bondholders, and that the railroad company was unable or unwilling to pay the interest upon its bonds, a federal court held that a receiver should be appointed.[1] The allegations of a bill filed by a bondholder, to foreclose a railway mortgage and for the appointment of a receiver, that the railway company had made default in the payment of taxes lawfully levied and imposed upon the railway property, and that, in certain counties, it had permitted its railroad to be sold for such taxes; and, further, that the company was hopelessly insolvent, and unable to pay its present and accruing indebtedness, and that it had failed, neglected and refused to pay wages and operating expenses and other obligations and indebtedness, amounting to more than $200,000, and the further allegation that the bondholder, upon these facts coming to his knowledge, had applied to the trustee named in the mortgage to take action, and that the trustee had failed and neglected to take any steps, were held in a federal court to make a case for the appointment of a receiver.[2] In a case where the same receiver of a rail-

[1] Farmers' Loan & Trust Co. *v.* Winona & S. W. Ry. Co., (1893) 59 Fed. Rep. 957.

[2] Putnam *v.* Jacksonville, Louisville & St. Louis Ry. Co., (1893) 61 Fed. Rep. 440. WOODS, Circuit Judge, said: "There is another phase of this growing indebtedness of the company in which the mortgagors or bondholders are interested. By the law as it has grown up under the case of Fosdick *v.* Schall, 99 U. S. 235, and later cases, establishing what is known in this circuit as the 'six months rule,' claims for labor and supplies, if not otherwise provided for, become entitled to preference over the mortgage debt. They, perhaps, do not constitute — I do not think they constitute — a lien on the property, such as to entitle the holders of them to apply for a receivership without first having established their demands. If such claims constituted a fixed or certain lien, their holders might be entitled to have receivers appointed to take care of their interests. But while there is not, strictly speaking, a lien, there is a preferential right which may be enforced against the mortgaged property if there be no other means of payment; and, consequently, to the extent that such demands are permitted to accumulate, the rights of the mortgagee are liable to be postponed. This bondholder, therefore, has a right to apprehend that his interest will suffer in that respect; and even if the delinquent taxes were paid, as it has been suggested they might be, that element of danger to his rights would not be eliminated.

road company had been appointed in an ancillary suit in one state, who had been appointed receiver in the original suit in another state, on principles of comity, there was a bill filed afterwards by the trustees under a mortgage to secure bonds issued by the railroad company for the appointment of a receiver, and for the foreclosure of the mortgage. It was shown in the United States Circuit Court for the district of South Carolina that the federal court in Georgia appointed its receiver at the instance of another railroad company that controlled the stock of the defendant company here, to further the interests of the dominant company's system, and not in the interest of creditors of the defendant company; and also that the federal court sitting in Georgia had since held that its action in the premises was unauthorized. The United States Circuit Court for the district of South Carolina held that, under these circumstances, a new receiver should be appointed, who could represent all interests, and whose position would be unassailable. Further, it was held that it was not necessary that the original receiver should be made a party to the trustee's bill, he being an officer of the court, and already within the jurisdiction and control of the court; nor was another corporation, against which charges were made, a necessary party, where no relief was asked against it.[1] A receiver having been appointed in a suit for foreclosure of a railroad mortgage, it has been held in Minnesota, constitutes no reason why a receiver should not be appointed in a proceeding by a judgment creditor of the railroad company under the laws of the state for the sequestration of all the property and effects of the corporation for the benefit of all its creditors.[2] There

I cannot escape the conviction that practically this road is insolvent, and to such a degree as to require the interference of this court."

[1] Phinizy *v.* Augusta & Knoxville R. Co., (1893) 56 Fed. Rep. 273.

[2] St. Louis Car Co. *v.* Stillwater Street Ry. Co., (1893) 53 Minn. 129; s. c., 54 N. W. Rep. 1064. It was said by the court: "The powers of the receivers in the two cases are entirely different. There are various classes of property that can be reached by a receiver under [the sequestration statutes] which could not be reached by a receiver appointed in a foreclosure suit. The former has substantially all the powers and functions of an assignee in bankruptcy. Everything becomes assets in his hands which are assets as to creditors, although not assets as to the corporation, as, for example, property conveyed in fraud of creditors, capital withdrawn without provision for the payment of corporate debts, the personal liability of stockholders, etc. Minnesota Thresher Mfg. Co. *v.* Langdon, 44 Minn. 37; s. c., 46 N. W. Rep. 310. Of course an appointment of a

was in a case a question as to the propriety of the United States Circuit Court for the northern district of Ohio appointing receivers of the property located within that jurisdiction. The court ruled upon this point that where a railroad receivership had been extended by ancillary appointment over the property of the company in its jurisdiction, the court could not, even if it had the power, extend the receivership to, or appoint additional receivers in, another independent and original suit brought by the corporation which had leased its road to the insolvent company, upon unsupported allegations that the original receivership was brought about by fraud and collusion, and that the receivers were hostile to the lease.[1] In a late case, the federal

receiver under [this statute] would not necessarily supersede the receivership in the foreclosure suit. If the court should be of the opinion that the interests of the mortgagee could not be otherwise properly protected, both receiverships might coexist; that under [the statute] being subordinate, as to the property covered by the mortgage, to the receivership in the foreclosure suit. And as it would be eminently desirable, if possible, that the entire property should be under the control of an officer of the court, there would be nothing improper in the court appointing the same person receiver in both cases, provided there is no conflict of interest between the mortgagee and the other creditors of the defendant."

[1] New York, P. & O. R. Co. *v.* New York, L. E. & W. R. Co., (1893) 58 Fed. Rep. 268. LURTON, Circuit Judge, said: "Whatever rights the complainant has as a creditor or under the lease it can set up as against the receivers without an extension of the receivership. Such extension would complicate accounts and result in conflicting directions. There are stronger reasons for the refusal to appoint additional receivers. The Erie system is a vast and extended one. Its lines extend into several states and as many different jurisdictions. The preservation of this system as a whole, its harmonious management as a unit, gives it its greatest value and power, and anything which tends to dismember it or to disrupt its management as an entirety should be avoided if possible. While it is a 'system' and while it remains a great 'trunk line' its management under order and direction of the court should be committed to one set of receivers having like authority in each jurisdiction and controlling each and every part of its property. Receivers are but officers and agents of the court. While necessarily much is committed to their judgment and discretion, yet their power depends upon the decrees and directions of the courts appointing them. Receiverships of railroads are in large part peculiar appointments. Railroads, as public carriers, are charged with great public duties, and the public are interested that their operation shall be continuous. Creditors are likewise interested that there shall be no cessation in their maintenance as going concerns, because their value as property depends upon the active use of the line. These considerations have developed the present well-settled proposition that such receivers are the mere custodians of the property, and hold

court for the eastern district of North Carolina, upon an intervention to rescind the order appointing the receiver of a railroad company, held that one possessing integrity of character, business experience, a capacity for the examination into and comprehension of accounts, who had had large financial experience and been concerned in the construction and management of railroads, with a knowledge of railroad accounts, was not disqualified to act as a receiver merely because he was not a railroad expert, acquainted with all the details of the mechanical work of a railroad plant. Neither should he be removed on the ground of alleged unfitness in removing the treasurer of the company and increasing the expenses of that office, of frequent visits in person on the railroad and extravagant expenditures, nothing being shown as to the ability of the person discharged, and the receiver's answer showing that the expenses of the treasurer's office had not been increased beyond what the pecuniary situation warranted; and the allegations of visits were positively denied by him, and no extravagant expenditure having been shown. Further, there was no disqualification of a person to act as receiver of a North Carolina corporation, owing its conception to the citizens of that state, merely because he was not a citizen of North Carolina.[1] In proceedings for the appointment of a receiver of an insolvent railroad company, one who is a party to or counsel in the cause,

for and as mere agents of the court. Speaking of the character of such trustees and the effect of such holding upon the interests procuring the appointment, Chief Justice WAITE said: 'The possession taken by the receiver is only that of the court, whose officer he is, and adds nothing to the previously existing title of the mortgagee. He holds pending the litigation, for the benefit of whomsoever in the end it shal be found to concern, and in the meantime the court proceeds to determine the rights of the parties upon the same principles it would if no change of possession had taken place.' Fosdick *v.* Schall, 99 U. S. 235, 251; Railroad Co. *v.* Humphreys, 145 U. S. 82; s. c., 12 Sup. Ct. Rep. 787. A receiver represents no particular interest or class of interests. He holds for the benefit of all who may ultimately show an interest in the property. He stands no more for the creditor than the owner. They are not assignees, and the principles of common law applicable to assignees do not define or determine the character of a receiver's possession or its effect upon the rights of those interested in the property in their possession. Receivers ought not to be appointed to represent the peculiar interests of one class, and, *a fortiori*, they should not be appointed to represent one interest out of a class of interests."

[1] Farmers' Loan & Trust Co. *v.* Cape Fear & Y. Val. R. Co., (North State Imp. Co., Intervener) 62 Fed. Rep. 675, confirming the appointment.

or who has been an officer of the company, will not be made the permanent receiver.[1] A United States circuit judge has authority to hear at chambers a motion to discharge a receiver of a corporation.[2] A federal court, which had been petitioned to remove a receiver of a railroad, has recently declared this rule of practice in such matters as a proper one. In general, the party who asks the court to remove one of its officers for malfeasance or incompetency should be prepared, not only to prefer specific charges of wrongdoing, but to accompany them with proof. It ought not to be tolerated that, upon mere vague and unsupported charges, one should be compelled to submit to a sweeping investigation into his conduct, and that upon such charges a court could properly be asked to order a general investigation into his conduct, and that upon such charges a court could properly be asked to order a general investigation to ascertain whether something might not be found objectionable to his standing. It is a fundamental and most just principle of law that one should not be put to answer vague and indefinite charges. Nor, in general, as to a specific charge of malfeasance, should one be put to his defense, in the absence of evidence tending to sustain the charge. In this particular case, the receiver objected to had been appointed at the request of the trustees in all but one of the mortgages on the railway, and on the recommendation of the bondholders secured by the mortgages, with the express assent of the railroad company, in the service of which he had been for many years as general manager of the railroad, and as director, vice-president and president. He was thoroughly familiar with its history, conditions and necessities, and was a thoroughly competent railroad manager. The proofs established that the road had been managed with prudence and economy, so far as concerned its actual operation, and no fault in the management of the property was

[1] Finance Co. of Pennsylvania *v.* Charleston, C. & C. R. Co., (1891) 45 Fed. Rep. 436.

[2] Walters *v.* Anglo-American Mortgage & Trust Co., (1892) 50 Fed. Rep. 316. CALDWELL, Circuit Judge, said: "The exercise of chambers jurisdiction in equity cases is absolutely essential for the purpose of preventing the delay, injustice, expense and inconvenience which must inevitably ensue if applications for relief had to be made in all cases to the court in session. A motion to discharge a receiver may be heard at chambers, upon direction, and will be granted when it appears that he was improvidently appointed, or that there is any other sufficient reason for his discharge. Railroad Co. *v.* Sloan, 31 Ohio St. 1; Crawford *v.* Ross, 39 Ga. 44; Beach on Rec. § 778.

suggested. The court declined to remove the receiver against whom the petition was directed, holding the fact that he was an officer and director of the company at the time of his appointment not to be a ground for a revocation of his appointment.[1] BOND, Circuit Judge, in the United States Circuit Court for the district of Maryland, while recognizing that the suggestions and recommendations of persons who substantially own property about to be intrusted to a receiver are of great weight with the court in making an appointment of a receiver, declined to remove this receiver of railway property, whose management had been able, efficient and impartial, at the request of the controlling stockholder and his associates, in a case where the litigation was not for the purpose of foreclosing a mortgage, but was instituted by a minority stockholder on the ground that the bonded indebtedness and the issues of stock were being vastly increased without any corresponding increase of assets, and mainly for the benefit of the controlling stockholder.[2] The removal or appointment of a receiver rests in the sound discretion of the court making the order, and is not reviewable in the Supreme Court of the United States.[3] A court of equity appointing receivers for a corporation, in case the parties interested fail to provide means for the discharge of such receivers within a reasonable time, will, on its own motion, consider the propriety of dissolving the receivership.[4]

[1] Farmers' Loan & Trust Co. *v.* Northern Pacific R. Co., (1894) 61 Fed. Rep. 546.

[2] Street *v.* Maryland Cent. Ry. Co., (1893) 58 Fed. Rep. 47.

[3] Milwaukee & Minnesota Railroad Co. *v.* Soutter, 154 U. S. 540; followed in Milwaukee & Minnesota Railroad Co. *v.* Soutter, 154 U. S. 541.

[4] Platt *v.* Philadelphia & Reading R. R. Co., 65 Fed. Rep. 872. Who should be appointed receivers, see Olmstead *v.* Distilling & Cattle Feeding Co., 67 Fed. Rep. 24; Ralston *v.* Washington & C. R. Ry. Co., 65 Fed. Rep. 557. When receivers will or will not be removed, see Etowah Mining Company *v.* Wills Valley Mining & Mfg. Co., (Ala.) 17 So. Rep. 522; Gypsum Plaster & Stucco Co. *v.* Adsit, (Mich.) 63 N. W. Rep. 518; Fowler *v.* Jarvis-Conklin Mortgage Trust Co., 66 Fed. Rep. 14. In Clap *v.* Interstate Street Ry. Co., (1894) 61 Fed. Rep. 537, COLT, Circuit Judge, denied a petition to appoint a separate receiver for one of the railway company's branches, such branch having ceased to be operated by reason of the destruction of its power house. He said: "If the road were running the court might, upon the showing made by the petitioners, direct the receiver to keep a separate account of the receipts and disbursements of [the branch road], but in the present condition of affairs, I see no necessity for making any such order. The burning of the power

§ 545. **Conditions attached to the appointment of a receiver.**— The doctrine of the United States Supreme Court is that a court of equity may make it a condition of the issue of an order for the appointment of a receiver that certain outstanding debts of the company shall be paid from the income that may be collected by the receiver or from the proceeds of sale; that the property being in the hands of the court for administration as a trust fund for the payment of incumbrances, the court, in putting it in condition for sale, may, if needed, recognize the claims of materialmen and laborers, and some few others of similar nature, accruing for a brief period prior to its intervention, where current earnings have been used by the company to pay mortgage debts or improve the property, instead of to pay current expenses, under circumstances raising an equity for their restoration; as, for instance, where the company, being insolvent and in default, is allowed by the mortgage bondholders to remain in possession and operate the road long after that default has become notorious, or where the company has been suddenly deprived of the control of its property, and the pursuit of any other course might tend to cessation of operation.[1] The better practice, it has been held, when a receiver has been appointed for a railroad, is for the judge of the court making the appointment to stipulate at the time, and as a condition of the appointment of a receiver, what debts and liabilities of the railway company shall be made a charge on the property and paid by the receivers. If the mortgagee is unwilling to take a receiver on the terms pro-

house has stopped the running of cars, much to the inconvenience of the public. If this had not happened, the effort might have been made to continue the road in operation while it remained in the hands of the court; but as this cannot be done, owing to this accident, I hardly think it within the legitimate powers of the court for it to undertake to set the road in operation again by the outlay of any considerable sum of money unless it should be requested so to do by all the parties in interest. It is not the business of the court to build railroads or to set railroads in operation which have ceased to run, but its duty is to preserve the property which comes into its hands until it passes to the rightful owners, and, incidentally, in furtherance of this end, to continue the operation of the railroad where it is practicable."

[1] Fosdick *v.* Schall, 99 U. S. 235; Miltenberger *v.* Logansport Railway, 106 U. S. 286, 311, 312; Penn *v.* Calhoun, 121 U. S. 251; Blair *v.* St. Louis, etc., R. R. Co., 22 Fed. Rep. 474; Farmers' Loan & Trust Co. *v.* Vicksburgh, etc., R. R. Co., 33 Fed. Rep. 778.

posed, the foreclosure can proceed without a receivership. If no order is made when the receiver is appointed, it can be made afterwards.[1]

§ 546. **Receiver's right as to possession of the property of the insolvent corporation.**—A court will protect its receiver in the possession and proper use and management of the property and privileges pertaining thereto committed to him. And it will extend such protection even to restraining another railroad company from proceeding to condemn, or to subject to its use, property in the possession of its receiver by proper legal proceedings, and will more readily do so when such condemnation or vice is sought or attempted to be had without any legal proceedings being taken for that purpose. In this case the court granted an injunction restraining a street railway company, its officers, servants and agents, from entering with their track upon, or in any manner interfering with, the right of way and roadbed of the street railroad as then possessed, used and operated by the receiver appointed by that court. At the same time the court refused to consider, at the instance of its receiver, who did not use electricity in his management of the street railroad in his

[1] Central Trust Co. *v.* St. Louis, A. & T. Ry. Co., (1890) 41 Fed. Rep. 551; Fosdick *v.* Schall, 99 U. S. 235; Blair *v.* Railroad Co., 22 Fed. Rep. 471. In Farmers' Loan & Trust Co. *v.* Kansas City, W. & N. W. R. Co., (1892) 53 Fed. Rep. 182, it appeared that there were many creditors entitled under the laws of Kansas to liens on the property, or parts of, it and also other creditors who had the right to subject the income and earnings of the road to the payment of their claims. The court required the trustee, as a condition of appointing the receiver, to assent to the payment of all their claims prior to the satisfaction of the bonds, and the decree appointing the receiver provided for the payment of all debts for ticket and freight balances, for work, labor, materials, machinery, fixtures and supplies of every kind and character furnished in the construction, extension, repair, equipment or operation of the road, and all liabilities incurred in the transportation of freight and passengers, including damage to person and property, which had accrued since the execution of the mortgage, CALDWELL, Circuit Judge, in the United States Circuit Court for the district of Kansas, held, that imposing this condition upon the appointment of the receiver was a proper exercise of the court's discretion to impose terms; and that the trustee's assent thereto was binding upon the bondholders, and the bondholders would not be permitted to become parties to the suit for the purpose of having this decree vacated. There is a very interesting and full note to this case on the foreclosure of railroad mortgages and matters pertaining to such suits in 53 Fed. Rep. 192, by Morris M. Cohn, of Little Rock, Ark.

possession, how the use of electricity by a competing company over five blocks of the same roadbed might affect future purchasers, should they desire to introduce that motive power.[1] The property of the railroad company involved in this foreclosure suit having been uninterruptedly in the possession of a succession of receivers appointed by federal courts for a length of time before the appointment of a receiver of the same property by a state court, the federal court refused to order the property transferred to the receiver appointed by the state court on his application for such an order, it appearing that the receiver last appointed by the federal court had actual physical possession under a bill filed by the trustee of bondholders representing the bulk of the indebtedness of the road, while the receivers of the state court represented only junior creditors, and but little of the indebtedness.[2] In the United States Circuit Court for the southern district of Georgia, the Central Railroad Company of that state, in a suit instituted by a stockholder and in which trust companies, as trustees of bondholders afterwards became parties, was placed in the hands of a receiver. This receiver was appointed under a bill alleging that the company which he had in charge operated and controlled several lines of railway, among

[1] Fidelity Trust & Safety Vault Co. *v.* Mobile St. Ry. Co., (1892) 53 Fed. Rep. 687.

[2] Central Trust Co. of New York *v.* Chattanooga, Rome & Columbus R. Co., (1894) 62 Fed. Rep. 950. It was said by the court: "The facts here make no such case as was made in the litigation over the Atlanta and Charlotte Air-Line railroad, in which conflicting opinions as to the duty of the courts as to possession of receivers were expressed by Justice BRADLEY and Circuit Judge WOODS, in the case of Wilmer *v.* Railroad Co., 2 Woods, 409; Fed. Cas. No. 17,775, or in the Atlanta & Florida Railroad case, in which a decision was made by the judge of the state court (not reported), and afterwards heard by Judge SPEER of the southern district, in the case of East Tennessee, V. & G. R. Co. *v.* Atlantic & F. R. Co., 49 Fed. Rep. 608. In both of these cases there was something of a race for the possession of the property, and the rule may be derived from these cases as well as from all the other authorities on the subject that the court which has the actual physical possession of the property will determine the justice and rights of its possession, and any other court appointing a receiver, even prior to the appointment by the court having possession, will direct that an application be made to the court in possession as to whether its receiver is rightfully entitled to possession. Under the facts stated as existing in the case at bar, a very different question is presented; the state court appointed its receiver, as has been stated, with the knowledge of the fact that the property was in the hands of the federal court, and notwithstanding that fact, and it did not direct its receiver to

others the Port Royal and Augusta Railroad Company; that the railroad company was unable to pay the interest on its bonds, and that a receiver was necessary in order to prevent dismemberment and disastrous litigation, and was placed in charge of these various properties. Afterwards one who was appointed receiver in the state court for the Port Royal and Augusta Railroad Company filed a petition in the federal court showing his appointment as receiver, etc., and praying that the receiver of the Central railroad and its subsidiary properties be directed to surrender the property of the Port Royal and Augusta Railroad Company to petitioner. The federal court granted the prayer of the petition and directed the surrender of the property to the receiver of the state court, holding that the Central Railroad Company being merely a creditor of the Port Royal and Augusta Railroad Company and a majority stockholder therein, but having no rights of ownership in the property of the road, had no right to its possession and control, and the receiver of the creditor company had no greater rights than the company itself.[1] An order appointing a receiver of a railroad company, among other things providing that "all the books, vouchers and papers touching the operation of the road" should be delivered by its officers, servants and agents to such receiver, has been held to include all the books relating to the previous history of the corporation and all records of its transactions, and not confined to books relating to the future operation of the road, or to such as the receiver might specifically demand, and an order of court appointing a receiver of a railroad company, providing for the delivery to the receiver of "all and every part of the properties, interest, effects, moneys, receipts, earnings, etc., embraces the company's seal.[2] LaCombe, Circuit Judge, in the United States Circuit Court for the southern district of New York, denied the motion of a stockholder for leave to inspect the books of a corporation which was in the hands of a receiver, it appearing that the applicant did not become a stockholder until six months after the receiver was appointed; at the same time it was declared by the court that in case a stockholder of a corporation in the hands of a receiver sought leave to

take possession, but, on the contrary, the effect of the order was to direct the receiver not to take possession."

[1] Central R. R. & Bkg. Co. of Georgia *v.* Farmers' Loan & Trust Co. of New York, (1893) 56 Fed. Rep. 357.

[2] American Construction Co. *v.* Jacksonville, T. & K. W. Ry. Co., (1892) 52 Fed. Rep. 937.

inspect its books, it would be no ground for denying him the right that his object was to obtain material to convince the other stockholders that a plan of reorganization which had met the approval of a majority of the stockholders should not be carried out. And while it would be proper for the receiver to refuse to allow such an inspection of the books of the corporation until it was ordered by the court, it was no part of his duty to promote one plan of reorganization as against another, either by opposing the petition to be allowed such inspection or otherwise, but he should remain absolutely neutral.[1] In a motion for an attachment for contempt in an action against a railroad company for the appointment of a receiver, and in which a receiver had been appointed by order of the court, it was held that a collection by the vice-president of the company, of money due the company under a mail contract, after the appointment of the receiver, and depositing this money in bank to the company's credit, and attempting to dictate what disposition the receiver should made of it, constituted contempt.[2] The mortgage containing a provision that the mortgagor shall remain in possession until default, a receiver appointed in an action for its foreclosure will have no right to earnings of the railroad corporation prior to the filing of the bill for foreclosure, though not paid until after his appointment.[3]

§ 547. The relation of the receiver to property leased by the corporation coming into his hands.— In this case an oil company manufacturing oil contracted with a railway company to purchase a certain amount of rolling stock, and lease it to the railway company at an agreed rental, the railway company agreeing to purchase the rolling stock on or before an appointed day, and pay for it in cash, or if it should be unable to do so to turn it over to the oil company at the expiration of the contract, in good order and condition. There was a further agreement that the charges for freights carried by the railway company in transportation for the oil company, might be applied to the payment of the rental and of the purchase money. The railway company was insolvent, and, before the expiration of this contract for rolling

[1] Chable *v.* Nicaragua Canal Construction Co., (1894) 59 Fed. Rep. 846.

[2] American Construction Co. *v.* Jacksonville, T. & K. W. Ry. Co., (1892) 52 Fed. Rep. 937.

[3] Hook *v.* Bosworth, 64 Fed. Rep. 443; s. c., 12 C. C. A. 208.

stock, in proceedings instituted by mortgage bondholders for foreclosure of their mortgage, was placed in the hands of a receiver, who continued to use the rolling stock. There was an intervention in the foreclosure suit by the oil company seeking to recover the balance of the purchase money from the receiver, and to secure the carrying out of the contract by him, and the retention of the amount of charges for freights due from the oil company, and their application to the payment of the rent and purchase money. The receiver answered the petition of the intervener, declining to complete the contract, and averred that the rental had been paid in full, and that there was a balance due him for freight. He also filed a cross-petition to recover the surplus. There was a provision in the contract between the lessor and lessee that if the latter, the railway company, became unable to pay its current debts in the ordinary course of business, it should be released from its obligation on returning the property. The United States Supreme Court held that the receiver had the right to return the property upon complying with the terms of the contract in respect to its return.[1] No part of the expenses of a

[1] Sunflower Oil Co. *v.* Wilson, (1892) 142 U. S. 313. Mr. Justice Brown, speaking for the court, said: "The case is not unlike that of Express Company *v.* Railroad Co., 99 U. S. 191. In that case, the express company agreed to loan the railroad company twenty thousand dollars upon its notes, to be expended in repairs and equipments. In consideration of this, the railroad company agreed to provide the necessary privileges and facilities for the transaction of all the business of the express company over its road; and to charge a certain sum for transportation, which was to be credited monthly toward the payment of the loan, with a proviso that if the loan was not paid within a year the contract should continue in force for a further period, or until the whole had been repaid. A mortgage upon the road having been foreclosed, the receiver repudiated the contract, forbade the express company from further using the cars of the railroad company unless upon conditions whereby the contract was virtually surrendered or ignored, and the express company was compelled to abandon the road, although the money loaned, with a portion of the interest thereon was still due and unpaid. It filed a bill for specific performance, alleging that the railroad company having conveyed away its property, and being in fact insolvent, the violation of the contract could not be compensated by any damages that might be recovered at law. This court dismissed the bill, holding that as the plaintiff had no lien and the contract was simply for the transportation of persons and property, the court could not require either a specific performance by the receiver, or the satisfaction of the plaintiff's demand of money; and that the express company had, therefore, no standing in a court of equity. The case of Coe *v.* New Jersey Midland Railway,

receivership, where a receiver has been appointed for the benefit of a railroad company and its creditors, can be properly charged to a company whose roadway was leased to the former.[1] The United States Circuit Court for the eastern district of Wisconsin has declared these rules: The appointment of receivers for a railroad system, and their taking possession of a leased line, does not of itself work an assignment or adoption of the lease, so as to make the receivers liable for the stipulated rentals. Receivers have, as a general rule, a reasonable time to determine whether they will adopt a lease, or will merely pay to the lessor the net earnings of its road, subject always to the lessor's right to enter for condition broken. But where the lessor immediately demands of the receiver and of the court either an adoption of the lease or a surrender of the road, and against its protest a decision was delayed for several months, in order to determine which policy was expedient, they held that the receivers should

27 N. J. Eq. 37, is also instructive in this connection. In that case, the Rhode Island Locomotive Works Company entered into an agreement with the railway company to furnish the latter certain locomotives and tenders, as upon lease, but with the agreement that, upon payment in full of the rent required, they should become the property of the railway. The rent was payable in installments, for which the company gave its notes; at the time of the appointment of the receiver there was due for rent about one hundred and twenty thousand dollars, and the locomotives were then in possession of the receiver and in use upon the road. Petitioners based their claim to relief upon the ground that the receiver requested them to leave the locomotives in his possession for use on the road, he guaranteeing to keep them in good order, and promising to apply for authority to pay the claim. In defense, the receiver alleged a notice by bondholders not to pay the rent or deliver the certificates therefor, which had been issued upon his application, because the property was not worth the amount agreed to be paid, and it was not for the interest of the trust that the rent should be paid. It was held that petitioners had no equity arising from the conduct of the receiver to have the contract specifically performed, without regard to the advantage or disadvantage of the trust fund; that, although they appeared to be willing, up to the time they were warned not to do so, to pay for the property according to their agreement, it might have been an improvident act on their part; that the fact that the receiver had applied for leave to issue the certificates to pay the rent did not bind them; and that the court would not grant the prayer of the petitioners until satisfied that it was for the interest of the trust that it should be done; but, that the petitioners would be allowed just compensation for the use of the property while held by the receiver."

[1] Brown *v.* Toledo, P. & W. R. Co., 35 Fed. Rep. 444.

equitably pay the full rental during the time of their possession.[1] This Ohio railroad company, the road of which constituted one of the leased lines of the Erie railway system, raised this same question as to the liability of the receivers of the Erie Company on account of the lease contract on its part of the Ohio road before the United States Circuit Court for the northern district

[1] Farmers' Loan & Trust Co. *v.* Northern Pac. R. Co. (Wisconsin Central R. R. Co., Interveners), (1893) 58 Fed. Rep. 257. JENKINS, Circuit Judge, first quoted from Oil Co. *v.* Wilson, 142 U. S. 313, 322; s. c., 12 Sup. Ct. Rep. 235, and then said: "In other words, when the court, upon the petition, and not the prayer of the complainant, appoints receivers, who are directed to take possession of the leased lines of railway operated in connection with the main line, such receivers take by order of the court, and do not, therefore, by the mere act of such possession, become assignees of the leases, they having, so to speak, a breathing space to determine whether or no they will assume the covenants of the lease. This is because of the necessities of the case. There is no other person to take immediate possession from an insolvent corporation in the interest of the public; and, as because of the public nature of the enterprise, the road must be kept a going concern; the performance of the duties of common carrier must not be permitted to be interrupted; the mails of the government must be transported; therefore, temporary possession is allowed to be taken; and, as a general rule, compensation for such possession must be measured by the terms of the instrument under which such possession was originally acquired and held. But that possession does not ordinarily operate to render the receivers assignees of the leases. Undoubtedly there are exceptions to the rule, arising because of the peculiar circumstances of the case, which equitably require the application of a different measure of compensation." The court regarded Railroad Co. *v.* Humphreys, 145 U. S. 82; s. c., 12 Sup. Ct. Rep. 787, such an exception, and distinguished it. He said: "There is, I think, a manifest distinction between that case and the one at bar. There the lessor, the inactive lessor, sought to obtain preference over a mortgagee not applying for the receiver; a lessor who sought to obtain rental pursuant to the terms of the lease when he was a party to the suit, and could have asked and would have received possession, but allowed the road for a long time to be operated by the receivers knowingly at a loss. Here possession of these leased lines was asked for by the trustees of the mortgage. The court was asked by the trustee to take possession of this leased line and operate it in connection with the main line of the defendant company as a unit, and to keep and maintain in its integrity and operate the entire system of roads from Chicago to the Pacific. In other words, as plainly as language could state it, the trustee * * * asked the court to adopt this course, and to enter into possession and operate it in the interest of the bondholders. In the Quincy case the bill was filed by the insolvent company. It was unable longer to continue the operation of the road, and petitioned the court, in the interest of every one interested, as well as its own interest, to take possession of the leased lines, and the lessors were parties to that suit. And the lessors, under the circumstances, without ap-

of Ohio. This latter court held that the receivers of a railroad company have no power to abrogate a valid lease of railroad property made to the company by another company, and, as between lessor and lessee, the lease must stand until abrogated under some of the conditions contained in the lease. Further, the mere appointment of receivers for a railroad company embracing a system of leased lines, and their taking possession of a leased road, did not, even if the bill showed that the receivership was brought about for the purpose of preventing a disintegration of the system, render the receivers assignees of the lease, or require the adoption of the lease by them, so as to make the rental a preferred claim which they were bound to discharge; neither did the fact that they continued to operate the leased line for some time work an adoption of the lease, when the lessor had never demanded a surrender of its road, although entitled to do so because of breach of condition by non-payment of rent. And rental accruing under a railroad lease prior to the appointment of receivers for the lessee was held to be an unsecured liability entitled to no priority to the mortgage bondholders.[1] A railroad company, in the hands of receivers, had been operating another company's road for several years under a lease by the terms of which it was to pay as rental thirty-two per cent of the gross

plication to the court for possession, allowed the road to be operated from May 29, 1884, to July 15, 1885, by the receivers at a loss to its knowledge, and without the slightest attempt to obtain possession. It could well have been held in that case that such action or non-action of the lessor would be held in equity to be an assent to the operation of that line by the receivers. But here possession was not only taken at the request of the trustee of the mortgage, upon the assertion that the severance of the trunk line to Chicago would result in ruinous sacrifice, but it has been continued against the continued protest of the lessors, who, almost from the date of the filing of the bill, have sought to compel the receivers to determine whether or no they will retain possession, adopting the lease, and if not, that possession should be surrendered to the lessors; and, also, when delay became inevitable, by the demand and act of re-entry they put themselves in the legal position where they could lawfully require the surrender of the premises, unless the court should, upon principles of equity, remove the forfeiture and allow the possession to continue in the receivers, adopting the lease and paying all past-due rentals. So that here the lessors have been continuously knocking at the door of the court demanding possession of the demised premises, and possession has been withheld from them against their consent and against their protest."

[1] New York, P. & O. R. Co. *v.* New York, L. E. & W. R. Co., (1893) 58 Fed. Rep. 268; agreeing with LACOMBE, C. J. Park *v.* New York, L. E. & W. R. Co., (1893) 57 Fed. Rep. 799.

earnings. It was also provided that a breach by the lessee company of any of its covenants should be cause of forfeiture, at the option of the lessor company, and that thereupon the latter might enter into possession of the property. When the receivers were appointed on the bill declaring the lessee company insolvent, the lessee was indebted for rental more than $300,000. The receivers had paid for the use of the property out of the assets more than that amount — a sum a little more than the net earnings of the leased property for the same period. The lessor company, in a petition to the court showing the importance to it of collecting promptly its rental in order to enable it to pay its obligations to its bondholders and to subordinate roads leased by it, asked that the court instruct the receivers to perform all the obligations of the lease, and to pay the rent then due; that, if without money to make the payment, the receivers be ordered to issue receivers' certificates for all rent due or to become due, these certificates to be deemed a charge and lien upon the property of the lessee company in the possession of the court through its receivers, prior to the outstanding mortgages of the lessee company. The petition did not ask a forfeiture of the lease for covenants broken. The United States Circuit Court for the southern district of New York, considering the petition, held that the receivers did not, by taking possession under the order of the court, become assignees of the terms of the lease, committed to the obligation, in any event, to pay the full sum stipulated as rental by the lease; neither had they retained possession for such an unreasonable time, or under such circumstances, as amounted to an election on their part to accept the lease; and it appearing that more than the net earnings of the leased property for the period during which the receivers had been in possession of it had been paid to the lessor, the court declined to instruct the receivers to pay any more out of the general *corpus* of the property in their hands.[1]

[1] Park *v.* New York, L. E. & W. R. Co., (1893) 57 Fed. Rep. 799; citing on the first point Quincy, etc., R. Co. *v.* Humphreys, 145 U. S. 82; s. c., 12 Sup. Ct. Rep. 787; St. Joseph, etc., R. Co. *v.* Humphreys, 145 U. S. 105; s. c., 12 Sup. Ct. Rep. 795; on the second point, Miltenberger *v.* Railway Co., 106 U. S. 286; 1 Sup. Ct. Rep. 140; Kneeland *v.* Trust Co., 136 U. S. 101; s. c., 10 Sup. Ct. Rep. 950; Central Trust Co. *v.* Wabash, etc., R. Co., 23 Fed. Rep. 863; 34 Fed. Rep. 259. When receivers will be held liable for the rent of a leased line and interest during the term of their receivership. Brown *v.* Toledo, P. & W. R. Co., 35 Fed. Rep. 444.

A receiver does not simply by virtue of his appointment become liable upon the covenants and agreements of a railway company of which he may be receiver.[1] Upon taking possession of property, for instance, leased to the company he is entitled to a reasonable time to elect whether he will adopt the contract under which it was leased, or whether he will insist upon the inability of the company to pay, and return the property in good order and condition, if the contract calls for that, paying, of course, the stipulated rental for it so long as he may have used it.[2] The court has power, in a foreclosure trial, on consulting the receivers, and without notice to the mortgagees, to order the lease of another road which is found necessary to the profitable management of the mortgaged property.[3] A receiver of a railroad embracing a leased road, cannot recover of the lessor road expenses incurred in running it, but is entitled to payment for betterments of its roadbed.[4]

§ 548. **Powers of receivers as to contracts, etc.**— The United States Circuit Court for the district of New Jersey, in which a creditor of a corporation of that state which had already been placed in the hands of a receiver by a court of the state brought his action against the receiver and others to set aside alleged fraudulent conveyances made by the corporation, held that he could not maintain the suit; for, as the New Jersey statute relating to corporations vested the receiver with all the rights and equities of the creditors, the receiver alone could enforce them. Further, the mere refusal of the receivers to act did not authorize the creditor to sue in person, as the statute of New Jersey gives to any person aggrieved by the receiver an appeal to the chancellor who appointed him. Besides, a creditor of a business corporation which had been placed in the hands of a receiver could not, without leave of the court appointing him, maintain a suit in another court to set aside fraudulent conveyances of the corporate assets. Furthermore, a creditor having a claim of less than $2,000 against an insolvent corporation, suing for himself alone, could not maintain the suit in a Federal Circuit Court on

[1] Hoyt *v.* Stoddard, 2 Allen, 442.

[2] Turner *v.* Richardson, 7 East, 335; Commonwealth *v.* Franklin Insurance Co., 115 Mass. 278; Sparhawk *v.* Yerkes, 142 U. S. 1.

[3] Mercantile Trust Co. *v.* Missouri, K. & T. Ry. Co., (1889) 41 Fed. Rep. 8.

[4] Phinizy *v.* Augusta & Knoxville R. R. Co., 56 Fed. Rep. 273.

the ground of diverse citizenship, notwithstanding the fact that he sought to set aside fraudulent conveyances of corporate assets greatly exceeding $2,000 in value.[1] The receiver of the property of a railroad company may terminate at will an arrangement which he has made for the transportation of the freight and passengers of another railroad company over the line of road under his control, where there is no provision making the arrangement obligatory on either party for any stated period of time, without previous notice to the other company.[2] The receiver of a railroad in Florida, where discrimination in freight rates is a criminal offense, has no right to make such discrimination.[3] On a petition

[1] Werner *v.* Murphy, (1894) 60 Fed. Rep. 769. In the opinion GREEN, D. J., gives full consideration to the law of New Jersey governing receivers under the jurisdiction of its laws and courts.

[2] Investment Co. of Philadelphia *v.* Ohio & N. W. Ry. Co., (1889) 41 Fed. Rep. 378.

[3] Cutting *v.* Florida Ry. & Nav. Co. (Mallory et al., Interveners), (1890) 43 Fed. Rep. 747, following Missouri Pac. Ry. Co. *v.* Texas & Pac. Ry. Co., 31 Fed. Rep. 862. What kind of contract with reference to transportation of freight over railroad in his possession a receiver cannot make, see International & G. N. R. Co. *v.* Wentworth, (Tex. Civ. App. 1894) 27 S. W. Rep. 680. In Seibert *v.* Minneapolis & St. L. Ry. Co., (Minn. 1894) where two railroad companies agreed that each should construct or cause to be constructed a specified part of a continuous line of railroad between two terminal points and make certain connections, and that each should have the concurrent use of the whole line and have certain other traffic arrangements with the other, and that this contract should be in force for a certain number of years, the line was so constructed, and, after being so used for some time, a receiver of one of said companies was appointed in a foreclosure suit brought against it. The other company presented a claim for rent, switching charges, expense of handling freight and other operating expenses accruing to it under the contract before the receiver was appointed, and the court below ordered the payment of the same by the receiver with interest. The Supreme Court of Minnesota held that it was proper to order the payment to be made, it being fairly to be inferred from the order of the court and other proceedings that the court deemed this contract a valuable asset, and deemed it for the best interest of the estate that the receiver should adopt the contract, and that it was necessary to pay the claim in order to keep the contract in force. In Central Trust Co. *v.* Marietta & North Ga. Ry. Co. (Blue Ridge Marble Co., Intervener), (1892) 51 Fed. Rep. 15, it appeared that the railroad company contracted with the intervener to carry marble from one point to another and allow the same to be stopped over at an intermediate point to be dressed and then reshipped and carried to a terminus of the road without extra charge, the entire charge for freight being paid in advance. The United States Circuit Court held that the receiver appointed in this suit of the bondholders to foreclose their mortgage on the railroad could not be com-

by contractors against the receivers of a railroad to secure payment for the erection of a building, the court referred the cause to a master to ascertain the amount "justly and equitably due as the true value of the work done and material furnished." The master found the work was done under a contract between the receivers and the builders, refused to hear evidence as to value, and reported the contract price as the amount due. The court, after a hearing on exceptions, confirmed the report and entered judgment thereon. It was held by the United States Circuit Court of Appeals for the eighth circuit that while the order of reference was open to the construction that the actual value of the work and material was to be ascertained, yet, as the trial court had held that it was not intended to bear so broad a construction, and had confirmed the report, an appellate court would not be justified in holding the contrary where no injustice had resulted. These facts appeared in the case: That while these railroad buildings were in course of construction a foreclosure suit was instituted against the company, and two receivers appointed. Shortly after their appointment, by a joint letter, the receivers notified the contractors to stop work, stating that they would later furnish designs and directions for completing the work, and in the letter said: "And you will name a gross sum for the performance of the same, which will be submitted to the court for approval." New plans and specifications were then prepared and approved by the court, and an order was entered directing that the buildings be completed in accordance therewith. The receiver in active charge of that portion of the road notified the contractors of this order, and soon afterwards they answered by letter submitting a bid for which they would complete the work on the new plans. The active receiver testified that the receivers accepted the bid, and that a formal contract was prepared and was signed by the contractors, but was never signed by the receivers. Relying on this contract the contractors completed the work. The other receiver testified that he knew nothing of the bid, but that he afterwards saw the work going on, and assumed it was with his colleague's concurrence, and without any estimates or contract. The Court of Appeals held that these facts were sufficient to justify the mas-

pelled to transport the marble on the terms of this contract, although the freight had been paid for such transportation before the appointment of the receiver. Following Express Co. *v.* Railroad Co., 99 U. S. 191.

ter in finding that the work was completed under a binding contract with the receivers.[1] Where a bill was filed by the president and directors of a railroad company, alleging that as a result of an unlawful lease and the diversion of its income it had been embarrassed; that if properly managed it might extricate itself from its difficulties, and the court appoints its president receiver for the purpose of preserving the property, and, with the aid of the court, placing it upon a prosperous footing, and no lien creditors are parties, it is competent for such president receiver, with the authority of the court, to pledge collateral and equitable assets of the company to secure loans necessary to its operation, and also to incur a liability for the expenses of a refunding scheme. If, however, before such expenses are paid, creditors holding liens upon the property are made parties, the court will not *ex parte* allow the expenses of such refunding scheme to be paid by the receiver.[2] A receiver of a railroad, appointed with authority "to make all contracts that may be necessary in carrying on the business of said railroad, subject to the supervision [of the] court [appointing him]," has no authority to make a lease for a term of general offices, without authority from that court, and to bind his successors and the property therefor for the term, without direction from or sanction by the court. Further, the Supreme Court of the United States held that the facts that the receiver's accounts showed, monthly, the payment of the rent of such a lease, and that that rent was reasonable, and that the accounts as rendered were passed by the master and reported to and approved by the court, did not amount to a sanction of the lease for the term.[3] This insolvent railroad company, as assignee of another

[1] Girard Life Insurance, Annuity & Trust Co. *v.* Cooper, (1892) 51 Fed. Rep. 332. When proper to extend the receiver's powers, see Mercantile Trust Co. *v.* Missouri, Kansas & Texas Ry. Co., 41 Fed. Rep. 8. When an application of the trustees of an underlying mortgage to have the property of the company turned over to a receiver appointed in their suit to foreclose by a receiver of the whole system of roads should be denied, see Central Trust Co. *v.* Wabash, St. Louis, etc., Ry. Co., 25 Fed. Rep. 693.

[2] Central R. R. & Bkg. Co. *v.* Farmers' Loan & Trust Co. of New York, (1893) 54 Fed. Rep. 556.

[3] Chicago Deposit Vault Co. *v.* McNulta, (1894) 153 U. S. 554. Mr. Justice JACKSON, in the opinion of the court, said: "In Cowdrey *v.* Galveston, Houston, etc., Railroad, 93 U. S. 352, it was held that a receiver is not authorized, without the previous direction of the court, to incur any expenses on account of property in his hands beyond what is absolutely essential to its preservation and use,

railroad company, held a half interest in a certain bridge and piece of track, the maintenance of which was provided for in a general contract with the other joint tenants. Receivers of the insolvent company, including its leased lines, among them the assignor railroad company's, were appointed and made a special contract for specific repairs, which were made by the joint tenant in accordance with this contract. Thereafter a special receiver was appointed for the assignor company. Upon the intervention of the joint tenant the federal court held that the receivers of

as contemplated by his appointment. Accordingly, the expenditures of a receiver to defeat a proposed subsidy from a city, to aid in the construction of a railroad parallel with the one in his hands, were properly disallowed in the settlement of his final account, although such road, if constructed, might have diminished the future earnings of the road in his charge. The same general principle is recognized in Union Trust Co. *v.* Illinois Midland Ry. Co., 117 U. S. 434, 479, where debts for considerable sums of money, borrowed by the receiver without previous authority from the court, were not allowed any priority out of the trust fund, although the moneys borrowed were applied to pay expenses of the receivership, such as supplies, repairs and pay rolls, and to replace moneys which had been so applied, for the reason that no order of the court had been obtained to borrow funds for those purposes. In Lehigh Coal & Navigation Co. *v.* Central Railroad, 35 N. J. Eq. 426, it was said that 'the receiver may undoubtedly appropriate moneys in his hands belonging to the trust to such purposes connected with the trust as he may think proper, always taking the risk that the court will finally approve his action; but he has no authority to bind the trust by contract without the authority of the court. Until his contracts are approved and ratified by the court the court is at liberty to deal with them as it shall appear just, and may either modify them or disregard them entirely. * * * All persons dealing with receivers do so at their peril, and are bound to take notice of their incapacity to conclude a binding contract without the sanction of the court.' This states the correct rule upon the subject, especially in respect to contracts involving large outlays, and which may extend beyond the life of the receivership. The same general rule is stated in Beach on Receivers, § 257, as follows: 'But a receiver is not allowed to exercise his discretion in applying the funds in his hands. These he holds strictly subject to the direction of the court, and only to be disposed of upon its order. Neither can he enter into contracts without the approval of the court. Although as receiver he may enter into negotiations and make such agreements as would be binding upon him as an individual, yet, in order to affect the fund in his hands, his acts must be ratified by the court. The rule is so well established that it has been decided that all persons contracting with a receiver are chargeable with knowledge of his inability to contract, and enter into contracts with him at their own peril, and that the court has unquestioned power to modify or even vacate his agreements.' To the like effect is a statement of the rule in section 186 of High on Receivers."

the insolvent company were liable as such for the repairs, though as against the assignor company they might have had a good claim therefor.[1]

§ 549. **Powers of the court and its receivers as to regulating wages of employees.**— Where the property of a railway or other corporation is being administered by a receiver under the superintending power of a court of equity, it is competent for the court to adjust difficulties between the receiver and his employees, which, in the absence of such adjustment, would tend to injure the property and to defeat the purpose of the receivership. It follows, then, that it is in the power of the court, in the interest of public order and for the protection of the property under its control, to direct a suitable arrangement with its employees or officers, to provide compensation and conditions of their employment, and to avoid, if possible, an interruption of their labor and duty, which will be disastrous to the trust and injurious to the public.[2] The power of a court appointing a receiver of a railroad corporation over such receiver's action, being under consideration, the United States Circuit Court for the northern district of Ohio declared these rules: The court appointing a receiver to carry on the business of the corporation necessarily commits to the discretion of the receiver the management of all administrative details relating to the business, and will not interfere with his management unless an abuse of his discretion is made to appear. In this particular case, upon the complaint by the receiver's employees in respect to a reduction of their wages, it was held that the court would not interfere to reverse the receiver's administration by settling the details of the complaints involving, as this would, an extensive investigation of administrative details, but, in case an abuse of discretion on the part of the receiver was made manifest, the court would select a new receiver, to whom such matters might more satisfactorily be intrusted.[3] The United States Circuit Court for the district of

[1] Central Trust Co. of New York *v.* Wabash, St. L. & P. Ry. Co. (St. Louis, K. & N. W. Ry. Co., Intervener), (1892) 52 Fed. Rep. 908.

[2] Waterhouse *v.* Comer, (1893) 55 Fed. Rep. 149, in which the court directed the receiver of the railroad to enter into an appropriate contract with the locomotive engineers in his employ, subject to the general opinion of the decision of the court with reference to rule 12 of the brotherhood.

[3] Consolidated Trust Co. of New York *v.* Toledo, St. L. & K. C. R. Co., (1894) 59 Fed. Rep. 514.

Washington declined to make an order that the receiver appointed by the court of a railroad company should conform to the terms of a certain contract made by the company with its employees prior to his appointment as receiver, whereby the employees were not to be discharged, except for cause, to be determined by arbitrators, holding that the receiver was not bound by such agreement.[1] The court here refused to confirm the action of the receivers of an insolvent railroad system in reducing the wages and changing the regulations for the conduct of its employees which were in force when the property came into the possession of the receivers, the employees affected not having been notified of the proposed changes, and given an opportunity to point out before the receivers any inequalities or injustice that would be caused by these changes.[2] It appeared here that, as the results of conferences beween the managers of this railroad company, certain rules, regulations and schedules, which had remained substantially unchanged for several years, determined mainly the relations between the company and its employees, as well as their rates of wages. That no change should be made in them or in the rate of wages without certain notice to the organization, the members of which would be affected, was one of those rules and regulations. The receivers appointed for this insolvent railroad company had a set of rules and regulations and schedules of wages prepared by themselves approved by order of the United States Circuit Court for the district of Nebraska, and authority was given them to put the same in force. The Circuit Courts of other districts through which the road extended having declined to give effect to the order in those districts,[3] the receivers applied to the Circuit Court for a rehearing before the Circuit judges. Upon this rehearing, the court held that the schedules of wages established for so long a time between the company and its employees must be presumed to be just and reasonable, and that the new and reduced schedules adopted by the receivers without notice to the employees or their representatives would not be approved by the court, although recommended by a majority of the receivers.[4] In another case

[1] In re Seattle, L. S. & E. Ry. Co.; Grievance Committee of Brotherhood of Railway Trainmen, Lodge No. 196, *v.* Brown, (1894) 61 Fed. Rep. 541.

[2] Ames *v.* Union Pac. Ry. Co., (1894) 60 Fed. Rep. 674.

[3] See Ames *v.* Union Pac. Ry. Co., 60 Fed. Rep. 674.

[4] Ames *v.* Union Pac. Ry. Co., (1894) 62 Fed. Rep. 7.

before the federal courts, it appeared that a railroad company, the property of which was the equipment and leasehold of another road, passed into the hands of a receiver. The annual rent was a first lien on the equipment, and the leasehold was subject to forfeiture for non-payment of the rent. The earnings of the road fell off, owing to general depression, until they were not sufficient to pay the rent. The receiver thereupon ordered a reduction of ten per cent in wages of all employees. Such a reduction, it also appeared, had been before then made by competing roads, and that the working time of each one of the employees had been lessened by the receiver in order to avoid a discharge of any of them. The Circuit Court held that this reduction was not unreasonable in such a case.[1] In the United States Circuit Court for the northern district of Georgia, the rule declared as to the proper treatment of employees of a railroad company operated by a receiver, in case of injury to those employees, is as follows: A person in the employ of a receiver having been injured while in the discharge of his duty, without negligence on the part of either, the court may properly order that his wages be paid to him for the time during which he continued disabled, the view of the court being that the officers of the court should be required to act towards their employees as persons of ordinary humanity and right feeling would act under similar circumstances. The usual rule was, however, limited in this wise: The compensation should be confined to faithful and deserving employees and to those who merit such consideration.[2]

§ 550. Receiver's certificates — when they will be authorized — the lien of such certificates and its enforcement.— Here the receiver had been appointed on the petition of a comparatively small holder of stock in a small local narrow-gauge railroad company. The court which had appointed him refused to authorize him to issue receiver's certificates to provide for new equipment, additional sidings and permanent structures, in order to test its earning capacity if fully developed, as the issuing of such certificates was opposed by all other interests, and the

[1] Thomas *v.* Cincinnati, N. O. & T. P. Ry. Co., (1894) 62 Fed. Rep. 17.

[2] Thomas *v.* East Tennessee, V. & S. Ry. Co. (Cook, Intervener), (1894) 60 Fed. Rep. 7, limiting rule in Missouri. Pac. Ry. Co. *v.* Texas & P. Ry. Co., 33 Fed. Rep. 701; 41 Fed. Rep. 319.

first mortgage bondholders were pressing for a foreclosure of their past due mortgage; it was furthermore apparent that the road could not in any reasonable time cancel the certificates, and resume payment of interest on its bonds, and that the first measure of the new owners would be to change the road to a standard gauge, thus rendering the proposed improvements useless.[1] It was held in this case, where a receiver of a railroad had been appointed on the petition, not of the bondholders, but of a stockholder, and no earnings had been diverted to pay interest on bonds, there was no lien or equity requiring the payment of past-due labor and material claims out of the *corpus* of the property by the issuance of receiver's certificates. But there was, however, an equity requiring payment of those whose labor actually kept the road a going concern out of any net earnings which the receiver might realize, but such earnings could not be anticipated by raising money on receiver's certificates except by agreement of the parties.[2] Should all parties consent that the receiver of a railroad company, though not engaged in operating the road, be, and he is authorized by order of court to issue certificates which shall constitute a lien on the company's property superior to certain prior mortgages, and the money obtained on such certificates is used in preserving and improving the property, the purchasers of the property at a subsequent sale to foreclose said mortgages are estopped from denying the validity of the certificates.[3] The order for certificates of the receiver in this case, on his *ex parte* application had been modified so as to declare some of the certificates invalid, with the privilege to the holders of such certificates to intervene in the suit and have their validity adjudicated. It was held that a petition in intervention by such certificate holders, which recited the modified order, did not thereby admit the invalidity of the certificates; nor did the fact that the principal of such certificates was not due make the intervention premature, if the interest thereon was then due and unpaid.[4] And the receiver who issued the certificates and who has in his hands the funds from which they should be paid, is a necessary party defendant to such intervention.[5] In a foreclosure

[1] Street *v.* Maryland Central Ry. Co., (1893) 59 Fed. Rep. 25.

[2] Ibid.

[3] Central Trust Co. *v.* Sheffield & Birmingham Coal, Iron & Ry. Co. (Anniston Loan & Trust Co., Intervener), (1890) 44 Fed. Rep. 526.

[4] Ibid.

[5] Ibid.

suit of a mortgage executed by a railroad company which received the railroad property by conveyance from a purchasing committee of bondholders of a former railroad company carrying out a plan of reorganization in their interest, the holder of receiver's certificates which, by order of the court in which the mortgage against the former railroad company was foreclosed, had been issued and sold to this holder, intervened by petition to enforce the prior lien of these certificates. The court declared these rules to be applicable in this case, to wit: The lien of receiver's certificates continues as long as the order authorizing their issuance remains in force, though such order was made without notice to parties interested; and the fact that a reference is had to determine all claims against the receiver, and a report is confirmed which makes no allusion to the certificates, is not an adjudication against them, when it appears that they were not presented or considered, and that their holder had no notice of the reference.[1] Receiver's certificates, which are ordered to be paid out of the income of the road from time to time, are in the nature of call loans, and the holders have a right to presume that the receiver will notify them when the loan is to be called or the money paid. Where purchasers of receiver's certificates have paid their par value to the receiver, without notice of any facts to put them upon inquiry, their lien is not affected by the fact that the receiver appropriated the money to his own use.[2] It appeared in this intervention in a foreclosure suit, which was to enforce the payment of receiver's certificates against the purchaser of the corporation's property at foreclosure sale, that the president of the bank in which the receiver kept his deposits, having been authorized by the receiver to sell certain receiver's certificates, made the sale after his authority had been revoked, and caused the amount realized from the sale of certificates to be credited to the receiver on the books of the bank, and on the receiver's pass book. The receiver did not repudiate the sale, but, on the contrary, drew checks against the deposits, and reported the transactions to the court, which in the foreclosure

[1] As to the validity of the first lien of such certificates upon the railroad, see Wallace *v.* Loomis, 97 U. S. 146, 162; Union Trust Co. *v.* Illinois Midland Ry. Co., 117 U. S. 434; s. c., 6 Sup. Ct. Rep. 809; Vilas *v.* Page, 106 N. Y. 439. 451, 452; s. c., 13 N. E. Rep. 743.

[2] Mercantile Trust Co. *v.* Kanawha & Ohio Ry. Co., (1892) 50 Fed. Rep. 874.

decree recognized the validity of the certificates, and directed that the sale should be made subject thereto. The United States Circuit Court of Appeals for the fifth circuit held that the receiver was estopped to question the validity of the certificates as against an innocent purchaser. They also held the fact that the receiver, on afterwards learning that the bank was insolvent, demanded and received from the bank and from the president, personally, certain collateral securities, to protect his deposits, not to be a repudiation of the sale of the certificates, but rather a fresh ratification and acceptance of the deposits as the proceeds of the sale. The deposits representing the proceeds of the sale of certificates having been placed in the bank, by its president, in the form of checks, drafts, etc., on other banks, which were in fact duly honored by these other banks, the deposits must be held to have come into the receiver's hands, within the rule which makes the receipt of the proceeds by the receiver a condition precedent to the validity of the certificates, notwithstanding the fact that the bank was never in a condition to pay over any considerable proportion of the deposits to the receiver. Furthermore, the court, under the circumstances of this case, having recognized the validity of the receiver's certificates, and caused the foreclosure sale to be made subject to the lien of the certificates, was bound to recognize the estoppel of the receiver, as the court's agent, and to protect the innocent purchaser of the certificates by enforcing the same against the purchaser of the property.[1] The Court of Civil Appeals of Texas, in an action by a trustee of a corporation mortgage securing bonds to foreclose the same on lands of the corporation situated in that state, upon an intervention through which the holders of certain receivers' certificates which had been issued under order of a court of New York, in which proceedings to wind up this insolvent corporation incorporated in that state were pending, sought to have the certificates declared a prior lien, held that a court of another state having no jurisdiction to appoint a receiver for property situated in Texas, it could not authorize its receiver to issue certificates which should be a lien upon the property situated in Texas. Further, the fact that

[1] Alabama Iron & Ry. Co. *v.* Anniston Loan & Trust Co., (1893) 57 Fed. Rep. 25. See for the same principle as declared in the text, Levy *v.* Bank, 4 Dall. 234; Koontz *v.* Bank, 16 Wall. 196; Oddie *v.* Bank, 45 N. Y. 735; Bank *v.* Burkhardt, 100 U. S. 686.

in such case the president of the insolvent corporation attempted, under an order of the foreign court, to convey the property to the receiver, was immaterial.[1] It seemed that certain of the bondholders of this corporation had entered into an agreement with the purchasers of these certificates of the receiver of the New York court, that the certificates held by them should be a prior lien upon the lands in Texas. The Court of Civil Appeals affirmed the judgment of the court below that the rights of these purchasers of certificates could not be adjudicated under the agreement with these bondholders in the foreclosure suit without making those bondholders parties to the action.[2] The main question made in this case was whether the lien of the receiver's certificates upon the property of the former railroad company, against which the proceedings in foreclosure were conducted, in which these certificates were issued, had been discharged. The

[1] Pool *v.* Farmers' Loan & Trust Co., (Tex. Civ. App. 1894) 27 S. W. Rep. 744.

[2] Pool *v.* Farmers' Loan & Trust Co., (Tex. Civ. App.) 27 S. W. Rep. 744. The court said: "It is unquestionably true that in a number of cases the trustee appointed by the instrument creating the trust will be held authorized to represent the beneficiaries therein in suits involving the title to the trust property, as well as in the execution of the powers expressly conferred upon him. This is especially true where the parties are numerous, as in mortgages given to secure railroad bonds, and would include the mortgage given to appellee by the copper company in this case. * * * It will be observed, however, that the instrument relied upon in this case is not signed by the owner of the property, and no power is attempted to be conferred upon appellee, as trustee in the original mortgage, to represent them in reference to this contract, even by the bondholders who did sign it. It seems to be an agreement between appellants and the signing bondholders pure and simple. We think it clear that the agreement conferred no power upon appellee to represent the signing bondholders in reference to any of the matters embraced therein, for the simple reason that it attempted to give no such authority. We are, therefore, of opinion that these bondholders were necessary parties to a decree giving appellants priority over them by reason of the stipulations contained in that instrument." Citing Hudson *v.* Elevator Co., 79 Tex. 401; s. c., 15 S. W. Rep. 385. The court, as to how these purchasers of receivers' certificates might secure their rights, said: "As the proceeds of the sale under the judgment rendered by the court below will be paid to appellee, as trustee in the original mortgage, we see no reason why appellants cannot, in a proper proceeding in the New York courts, in which state all the parties are domiciled, have that part of such proceeds which would be due the bondholders who signed the instrument above set forth first applied to the discharge of these receivers' certificates, in compliance with its terms."

suggestion was that, by virtue of the sale and transfer of the railroad property to the purchasing committees of the bondholders in that suit, the lien was transferred from the property to the fund, which was paid into court in the foreclosure suit. It appeared that the decree confirming the rule directed the conveyance to be made expressly subject to the payment of any sums in cash on account of the purchase price which the court might afterwards direct, and a vendor's lien to be reserved for security. These provisions were incorporated in the deed to the committee of bondholders, and in their deed to the new corporation organized by the bondholders, the mortgage of which new corporation was here being foreclosed. The court held that the reservation had the force of a covenant running with the land, and, as no cash was paid in, the lien of the certificates was not transferred to the fund arising from the order, but was continued on the property.[1] It has been held that where receiver's certificates have been issued by the direction of a federal court in one state, and ancillary proceedings were had in a federal court of another state into which the road extended, the latter court had jurisdiction to enforce the lien of the certificates even in a separate suit and against a company which purchased the road after the sale in the original proceeding.[2]

§ 551. Rules as to claims against receiver growing out of rolling stock coming into his possession.— In a case before the United States Circuit Court of Appeals for the fifth circuit it appeared that an improvement company, interested in the con-

[1] Mercantile Trust Co. *v.* Kanawha & Ohio Ry. Co., (1892) 50 Fed. Rep. 874. It was said: "The precise point was adjudicated in Vilas *v.* Page, 106 N. Y. 439; s. c., 13 N. E. Rep. 743. ANDREWS, J., at page 454, 106 N. Y. Rep., and page 747, 13 N. E. Rep., says: "If the purchasers on the sale, whether bondholders or third persons, had paid the purchase money in cash, or secured its payment, there would, we conceive, be no doubt that the lien would be transferred to the proceeds. There would then be a substitute for the thing sold, upon which the lien would attach, relieving the land in the hands of the purchasers. But it could not have been the intention of the court to make a constructive payment on a purchase by the mortgagees, through a cancellation of the mortgage debt, equivalent to an actual payment, so as to relieve the property from the charge. Such a lien would be illusory merely, having no substantial quality. The purchasers cannot claim to have the premises purchased discharged from the lien."

[2] Mercantile Trust Co. *v.* Kanawha, & Ohio Ry. Co., (1892) 50 Fed. Rep. 874. The lien of receiver's certificates was enforced in an independent suit in Swann *v.* Clark, 110 U. S. 602; s. c., 4 Sup. Ct. Rep. 241.

struction of a railroad, and the president of which was a stockholder in the railroad company, and largely interested as a contractor in the construction of the railroad, equipped the railroad with rolling stock, and caused the same to be marked with the name of the railroad company; the improvement company's intent was to enable the company to issue certain bonds, secured by mortgage on its railroad as an equipped road, and such bonds were issued and placed through the instrumentality of the president of the improvement company. This was a suit by a holder of the bonds to foreclose that mortgage, and an assignee of the improvement company intervened, claiming the rolling stock. The Court of Appeals held that the improvement company and its assignee were estopped to allege that the transaction in question constituted a gratuitous loan of the rolling stock, or to deny the title of the railway company thereto, as against the bondholders.[1] The original vendor of this rolling stock, who, by his contract of sale to the improvement company, reserved title to the rolling stock, until payment of the purchase money, intervened in the same suit for foreclosure of the railroad mortgage on the railroad and its equipments which the improvement company had enabled the road to execute, as well as to negotiate its bonds. It was held by the same Court of Appeals that this original vendor of the rolling stock, having no notice of equities existing between the purchasers of the bonds of the railroad company and the improvement company, was entitled to the possession of the rolling stock, the title to which he had retained. But in such case, the improvement company, being estopped from setting up title against the bondholders by the fact that the bonds of the railroad company were placed through its instrumentality, the original vendor could take nothing by a resale to him by the improvement company of such rolling stock.[2] The rule was

[1] Central Trust Co. of New York *v.* Marietta & N. G. Ry. Co. (Hiawassee Co., Intervener), (1891) 48 Fed. Rep. 850, reversing Central Trust Co. of New York *v.* Marietta & N. G. Ry. Co. (Hiawassee Co., Intervener), (1891) 48 Fed. Rep. 32.

[2] Central Trust Co. of New York *v.* Marietta & N. G. Ry. Co. (Groome, Intervener), (1891) 48 Fed. Rep. 864, ordering the receiver to pay this vendor within a certain date the balance due him, or, if he was unable to pay, to deliver the property to him. There was a similar ruling in Central Trust Co. of New York *v.* Marietta & N. G. Ry. Co. (Jackson & Woodin Mfg. Co., Intervener), (1891) 48 Fed. Rep. 865, where there was a conditional sale to the improvement company of rolling stock.

declared by the United States Circuit Court of Appeals, in a case of foreclosure of railroad mortgage, where an intervener, who had furnished cars under a contract of conditional sale to the railroad company, and was held entitled to be paid balance of unpaid purchase money by the receiver, and the value of the rolling stock had been increased ten per cent since the same was furnished by him, that, in determining the sum which the receiver was to pay in order to retain possession of the rolling stock, ten per cent should be added to the cost thereof before deducting a percentage per annum for wear and tear.[1] The mortgage which was being foreclosed in this case covered "all after-acquired" as well as existing property of the railroad company, and was duly recorded. After its execution the railroad company purchased certain cars from a carbuilder, under an agreement by which the carbuilder retained title to the cars until they should be fully paid for, which agreement was in writing, but was never recorded. In the action for foreclosure of the mortgage the carbuilder intervened, claiming the cars under his reservation of title. The trust company foreclosing, opposed his claim, relying upon the effect of the statutes of Georgia concerning conditional sales. The United States Circuit Court of Appeals for the fifth circuit held that the trust company was not a third party within the meaning of the Code of Georgia, section 1955a (Laws 1881, p. 143), providing that, in order to retain title to personal property sold and delivered, as against third parties, "title must be reserved in writing, and the paper duly executed and recorded as a mortgage on personalty," and that the trust company could derive no advantage from the carbuilder's failure to record his reservation of title, as the statute was intended only for the benefit of subsequent purchasers and creditors of the vendee. Nor were the rights of the carbuilder affected as against the trust company, by the later statute of Georgia, which validates conditional sales of rolling stock to railroad companies with reservation of title, but requiring that such reservation shall be in writing, and shall be recorded within six months after the execution thereof, as that act was also intended only for the benefit of third parties, and operated to repeal the statute of 1881 no further than to provide a different method for the execu-

[1] Central Trust Co. of New York *v.* Sharp Co., Intervener), (1891) 48 Fed. Marietta & N. G. Ry. Co. (Jackson & Rep. 875.

tion of contracts for the conditional sale of railroad equipments.[1] It has been held by the United States Circuit Court of Appeals for the fifth circuit, in a suit for foreclosure of a railroad mortgage, that the statute of the state of Georgia, validating contracts for the sale of rolling stock made or to be made to the owner or operator of a railway within the state of Georgia, with reservation of title, and requiring such contracts to be recorded within six months after execution, had no application to such a contract, made before the passage of such act, by two foreign corporations, outside of the state, for the sale of rolling stock to be used within the state of Georgia, neither corporation being the owner or operator of a railway in the state.[2] The claim for rental of a leased line by the lessee company was pressed against the receivers of a railroad company of the system of which the leased line formed a part. This rule was declared: That the receivers of the system could not set off as against the claim for rentals accruing to the leased line during the receivership any cross-demand alleged to have accrued to the lessee prior to the receivership as the two claims arose in different rights. Further, in such case it was immaterial that the lessor was insolvent, when the lease provided for an arbitration of the matters claimed as a set-off, and expressly declared that the pendency of such arbitration should not interfere with the operation of the lease, and that all payments and transactions under the lease should continue exactly as if no controversy had arisen.[3] Where an insolvent railroad company, upon its own petition, procured the appointment of receivers to take possession of its road and leased lines, and in the same suit trustees of a mortgage asked, and were denied, an appointment of receivers, or an extension of the receivership under their cross-bill, but obtained a decree of foreclosure and a sale of the property thereon, it was held in the federal court that the rentals of the leased lines while in the possession of the receivers did not become a charge upon the *corpus* of the prop-

[1] Central Trust Co. of New York *v.* Marietta & N. G. Ry. Co. (Groome, Intervener), (1891) 48 Fed. Rep. 868.

[2] Central Trust Co. of New York *v.* Marietta & N. G. Ry. Co. (Jackson & Woodin Mfg. Co., Intervener), (1891) 48 Fed. Rep. 865. As to claims against receivers for the rental of cars, see Farmers' Loan & Trust Co. *v.* Chicago & A. Ry. Co., 42 Fed. Rep. 6; Kneeland *v.* American Loan & Trust Co., 136 U. S. 89; s. c., 10 Sup. Ct. Rep. 950.

[3] Farmers' Loan & Trust Co. *v.* Northern Pac. R. Co. (Wisconsin Cent. Co., Intervener), (1893) 58 Fed. Rep. 257.

erty to be paid in preference to the mortgage debt.[1] In a case in the United States Circuit Court for the northern district of Illinois, upon the intervention of a car company in a foreclosure suit brought by bondholders claiming rental for cars furnished to the company prior to the receivership, and to the receiver as they claimed after his appointment, Mr. Justice HARLAN declared this rule: On foreclosure of the railroad mortgage in this case, and the adjustment of claims of intervening creditors, the contract of lease of cars to the mortgage company, by the car company, dominated by the same persons, cannot be made the basis of an accounting for the use of the leased cars.[2]

§ 552. **Application of earnings of the road during receivership.**— Where the road of a railroad company, on application of second mortgagees, is placed in the hands of a receiver, after it has purchased on credit rails which were necessary for the purpose of keeping its road going, it has been held that the seller of the rails had an equitable right, as against the second mortgagees, to have the earnings of the road in the hands of the receiver applied first to the payment of his claim; but he had no such right against the first mortgagees, even though they had filed cross-bills in the suit, since they were not the ones who applied to the court of equity, and might, therefore, stand on their legal rights.[3]

[1] Central Trust Co. *v.* Wabash, St. L. & P. Ry. Co. (Swayne, Intervener), (1891) 46 Fed. Rep. 26.

[2] Thomas *v.* Peoria & Rock Island Ry. Co. (Western Car Company, Intervener), (1888) 36 Fed. Rep. 808. This was a foreclosure suit by bondholders, and, among other defenses of the petitioner to this intervention was that the controlling directors of the railroad company organized this car company for their own benefit, and, therefore, contracted with themselves, with intent to injure the bondholders. Upon this defense, the rule in the text was declared.

[3] Bound *v.* South Carolina Ry. Co., (1891) 47 Fed. Rep. 30. The reasoning of SIMONTON, J., to sustain his ruling, was as follows: "The Supreme Court has established that a railroad mortgage, so long as the road is kept a going concern, is a peculiar piece of property. The holder of a bond secured by such a mortgage takes it with notice that the earnings of the railroad, notwithstanding that they may have been specially pledged for his debt, must first be applied to the current expenses, labor, supplies, equipments and such permanent improvements as are absolutely necessary before they can be used for the payment of his interest. And, if perchance he be paid, leaving these or any of them unpaid, this would be a diversion of the fund, and a person holding any such exceptional claim has an equity under certain circumstances to be reimbursed by having such diversion corrected out of the income in the hands of the com-

Here a ferry company had a contract, by which a railroad company was to have the use of certain lands as approaches to the ferry, and on its part agreed to transport all of its freight and passengers over the ferry of this company, which was over a navigable stream. The railroad company, becoming insolvent, a mortgage it had given was foreclosed; it having been first placed

pany, and, if in the meantime a receiver has been appointed, out of the earnings in the hands of the receiver. This is an equity founded upon the doctrine that the officers of a railway company are trustees, or, perhaps, we should say, the recipients and holders of a trust fund, applicable first to claims of this character and after them to the interest on the mortgage debt. The origin and reason for this equity are found in the fact that a railroad is of public concern and must be kept up. Those who contribute to keep it up and so subserve the public weal are rewarded. This equity is enforced wherever suit is brought by the mortgagee to enforce his mortgage and is held superior to the legal lien of the mortgage. This doctrine was first distinctly set out in Fosdick *v.* Schall, 99 U. S. 235, and is sustained by a current of authority. Miltenberger *v.* Railway Co., 106 U. S. 286; s. c., 1 Sup. Ct. Rep. 140; Trust Co. *v.* Souther, 107 U. S. 591; s. c., 2 Sup. Ct. Rep. 295; Burnham *v.* Bowen, 111 U. S. 776; s. c., 4 Sup. Ct. Rep. 675. It seems to have been shaken in Kneeland *v.* Trust Co., 136 U. S. 89; s. c., 10 Sup. Ct. Rep. 950; but in Kneeland *v.* Foundry, etc., Works, 140 U. S. 592; s. c., 11 Sup. Ct. Rep. 857, the court quotes with approval Fosdick *v.* Schall and the authorities following it and reaffirms them. The only qualification laid down is that this equity is put in motion as to such claims only as arose within a reasonable time before the receiver was appointed. The term 'a reasonable time' is an unknown, or, perhaps, an uncertain quantity; at least it depends somewhat on the circumstances of the case and somewhat on the idiosyncracies of the chancellor. See Paine *v.* Railroad Co., 118 U. S. 159; s. c., 6 Sup. Ct. Rep. 1019. One of the cases fixes the limit at ninety days. Miltenberger *v.* Railway Co., 106 U. S. 288; s. c., 1 Sup. Ct. Rep. 140. In Thomas *v.* Railway Co., 36 Fed. Rep. 817, six months is selected as the limit. Judge BREWER, in Blair *v.* Railway Co., 22 Fed. Rep. 471, says that six months is the longest time within his knowledge that has ever been given. In the present case eighteen months elapsed between the purchase of the rails and the appointment of the receiver. But, as we have seen, this claim on the part of a materialman is protected by an equity. The officers of the company hold the earnings as a trust fund in which claims of this character have a preference. The payment of interest to bondholders, these material claims being unpaid, is held to be the use of money belonging to them for the benefit of others, and the diversion of the fund entitles them to recoup. It is difficult under these circumstances to see how any creditor of this class can be defeated in his application for reimbursement unless in analogy to the Statute of Limitations, or unless such circumstances exist as will induce the court to treat it as a stale claim, or unless he has lost an opportunity of recovering his debt from the company, or unless his *laches* has operated some change in the position of the mortgage creditor. At the time

in the hands of a receiver, its property was purchased by another railroad company, and this latter, having executed a mortgage securing bonds, becoming insolvent, a suit for foreclosure was instituted upon this mortgage and a receiver was appointed for its property. The purchaser of the property of the original contracting railroad company in part continued this contract with the ferry company, and so also did the receivers under the different foreclosures. The ferry company intervened in this last foreclosure suit and claimed that it should be, besides other relief asked, paid for certain rails which had been removed from the land by the receiver. The United States Supreme Court held that the ferry company was not entitled to recover the value of the rails removed by the receiver.[1] In a foreclosure suit involv-

this debt was incurred the whole railroad property, present and future, was covered by a statutory lien, by a first mortgage, a second mortgage and an income mortgage. The rails were absolutely necessary to keep the road a going concern. The Lackawanna Company furnished these rails, trusting to the statement of the president of the railway company that they would be paid out of the earnings. These belonged to the company (Fosdick *v.* Schall, *supra*), and the president could so dispose of them. The authorities quoted show that the Lackawanna Company belongs to a class of creditors who had an equity over these earnings even as against bondholders. When the notes first matured the railroad company had defaulted on its April and October interest of the second mortgage bonds. No action in the court on the part of the Lackawanna Company could have collected its claim. By pressure on the company it was paid one note. But, as the end of the struggle of the railroad company was inevitable, the Lackawanna Company had the right to rely upon its equity and to look for payment out of the diverted funds. It seems to me that this claim comes within the principle and the protection of Fosdick *v.* Schall."

[1] Wiggins Ferry Co. *v.* Ohio & Mississippi Ry. Co., (1892) 142 U. S. 396. It was said in the opinion: "In the case of Wagner *v.* Cleveland & Toledo Railroad, 22 Ohio St. 563, it was held that the stone piers built by a railroad company as part of its road on lands over which it had acquired the right of way, did not, though firmly imbedded in the earth, become the property of the owner of the land, as part of the realty, and that, upon the abandonment of the road, the company might remove such structures as personal property. So, in Northern Central Railroad *v.* Canton Co., 30 Md. 347, it was held that rails fastened to the roadbed of a railroad, as well as the depots and other buildings, might, under certain circumstances, be treated as trade fixtures, and removable by the company, if the surrounding circumstances showed that at the time the rails were laid upon the land, it was not intended that they should be merged in the freehold. In that case the road was built upon land under a license and permission of the owner. It is entirely clear that the suits in the case under consideration did not become part of the realty, and that the receiver was not guilty of waste in removing them from the land." When preferred debts for labor and

ing the mortgage of a street railway company, the United States Circuit Court for the northern district of California refused to direct the receiver to pay out money in his hands for the purpose of grading and macadamizing the street along and between the rails, in accordance with an order of the town trustees upon the ground that there was no lien in favor of the town for such an expenditure.[1] A railroad company operating a system of leased roads through several of the states was placed in the hands of a receiver in the federal court for the eastern district of Virginia. One who had furnished materials that were used in the roadbed of one of these leased roads which was operated as part of the system of the lessor road, proceeded in the state court against the lessor road

materials furnished, for the operation of a division of a system of railroads owned by a railroad corporation, are a lien upon the earnings of all the roads of the system prior to underlying and general mortgages, see Central Trust Co. *v.* Wabash, St. Louis, etc., Ry. Co., 30 Fed. Rep. 332. When the earnings of a system of railroads in the hands of a receiver may be expended in a greater proportion on some of the liens than on others, if necessary to the prosperity of the whole system, see Central Trust Co. *v.* Wabash, St. Louis, etc., Ry. Co., 30 Fed. Rep. 332. When a receiver should pay coupon bonds overdue in preference to coupons of bonds issued under a mortgage of a prior date, see Park *v.* New York, Lake Erie & Western R. R. Co., 64 Fed. Rep. 190. When a receiver will not be directed to pay out of the earnings in his hands interest on bonds secured by mortgage on a part of the road, merely to avoid foreclosure proceedings of the mortgage, see Cleveland, C. & S. R. R. Co. *v.* Knickerbocker Trust Co., 64 Fed. Rep. 623. That coal used in operating a road before and after receivership, should be paid for out of the surplus where income is insufficient, see Clark *v.* Central R. R. & Bkg. Co. of Georgia, 66 Fed. Rep. 803; s. c., 14 C. C. A. 112. When a receiver will be compelled to restore funds diverted by paying earnings to interest on bonds for the purpose of payment of taxes on property in his hands, see Clyde *v.* Richmond & Danville R. R. Co., 63 Fed. Rep. 21. For a declaration of rules by Mr. Justice HARLAN as to what is chargeable to income during receivership, see Thomas *v.* Peoria & Rock Island Ry. Co. (Western Car Co., Intervener), (1888) 36 Fed. Rep. 808–818; citing Fosdick *v.* Schall, 99 U. S. 235, 252–254; Milterberger *v.* Railway Co., 106 U. S. 286, 311, 312; s. c., 1 Sup. Ct. Rep. 140; Trust Co. *v.* Souther, 107 U. S. 591; s. c., 2 Sup. Ct. Rep. 295; Trust Co. *v.* Railway Co., 117 U. S. 434; s. c., 6 Sup. Ct. Rep. 809; Burnham *v.* Bowen, 111 U. S. 776; s. c., 4 Sup. Ct. Rep. 675; Trust Co. *v.* Morrison, 125 U. S. 591; s. c., 8 Sup. Ct. Rep. 1004; Railroad Co. *v.* Cowdrey, 11 Wall. 459; Gilman *v.* Telegraph Co., 91 U. S. 603; Bridge Co. *v.* Heidelbach, 94 U. S. 798; Sage *v.* Railroad Co., 125 U. S. 361; s. c., 8 Sup. Ct. Rep. 887; Trust Co. *v.* Shepherd, 127 U. S. 494; s. c., 8 Sup. Ct. Rep. 1250.

[1] Union Loan & Trust Co. *v.* Southern Cal. Motor Road Co., (1892) 49 Fed. Rep. 267.

and reduced his claim to judgment, after the lease was annulled as to this leased road. Pending the action, the receivers were appointed for the whole system. As to this judgment, it was held in the federal court for the district of South Carolina, where this intervention was made, that the judgment could not operate as a judgment against the receivers, nor bind the realty in their hands, it not having been in existence when they were appointed. A question was raised as to the jurisdiction of this intervention, as the intervener prayed of the court sitting for South Carolina, that his claim be paid out of income in preference to any mortgage lien, as being for materials that had assisted in keeping the system a going concern. The receivers of the lessor road were originally appointed in Virginia, and by these ancillary suits in the different states their authority was extended and confirmed. SIMONTON, D. J., of the United States Circuit Court for South Carolina, held that the court which originally appointed the receivers was the forum in which the claimant should seek relief. But, as he regarded the claim a meritorious one, he did not order the petition before him dismissed, but retained it, in order, if possible, to assist the petitioner in enforcing its payment.[1]

§ 553. **Jurisdiction of actions against receivers.**— The act of congress of 1887–1888, permitting receivers of railroad corporation property to be sued for acts or transactions of theirs in carrying on the business connected with the property, without leave of the court appointing them, does not confine those bringing the suits to the courts having jurisdiction of the receiver and the property, or to the federal courts generally. They may be sued, without such leave of court, in any court of competent jurisdiction. Neither is there any power in the court appointing them to enjoin the bringing of such suits in such other courts of competent jurisdiction.[2] But garnishment proceedings have been

[1] Clyde *v.* Richmond & Danville R. Co., (1893) 56 Fed. Rep. 539; Ex parte Powell, (1893) 56 Fed. Rep. 539.

[2] Central Trust Co. of New York *v.* East Tennessee, V. & G. Ry. Co., (1894) 59 Fed. Rep. 523. LURTON, Circuit Judge, after referring to cases prior to the passage of this act of congress, such as Davis *v.* Gray, 16 Wall. 218; Barton *v.* Barbour, 104 U. S. 126, and others, said, *arguendo:* "Whether it was the intention of congress to permit receivers appointed by, and accountable to, United States courts to be sued with respect to acts and transactions as such receivers in courts of

held not to be suits against the receiver for "any act or transaction of his," within the meaning of that act of congress, and the court appointing the receiver, it was also held, might enjoin the bringing of such proceedings, as well as suits upon causes of action originating before the receivership, and all other suits not arising from some act or transaction of the receiver in carrying

other jurisdictions, is by no means clear. Under the law as it stood the court, having custody of the property *pendente lite*, had exclusive jurisdiction of all suits affecting such property, and drew to itself complete jurisdiction with respect to all the acts and transactions of the receiver in maintaining or operating property so sequestrated. It was just as much a contempt of court to institute a suit affecting such property or its custodian, as such, in the court of his appointment, without previous leave of court, as it was to bring such suit in another jurisdiction. A judgment against the receiver is a judgment against the receivership. It is a judgment affecting the property and to be paid therefrom. To properly administer a sequestrated property the liabilities should be determined in due course and the claims ranked, and the property marshaled and distributed according to legal or equitable priorities. The act might well have been construed as only permitting suits in the court having jurisdiction of the property and the receiver. This would have secured to the suitor the right of jury trial, according to the usual course of the court, where the demand was of legal character. At the same time such judgment would have been subject to the equitable jurisdiction of the court, and be given its proper rank in the distribution of the property. There is much force in the argument that, in view of the previous exclusive jurisdiction of the court appointing the receiver over him and over the sequestrated property, a construction ought to be given this act which would have preserved the equitable jurisdiction of the Circuit Courts over property in *custodia legis*, and over suits affecting it. We, however, feel precluded from now placing such a construction upon the act in consequence of the decisions of the Supreme Court of the United States in McNulta *v.* Lochridge, 141 U. S. 327; s. c., 12 Sup. Ct. Rep. 11; Railway Co. *v.* Johnson, (1894) 14 Sup. Ct. Rep. 250. * * * If that act authorized a suit against a receiver in a state court, without leave of the court appointing the receiver, in respect to a liability incurred while carrying on the operation of a railroad as a receiver under a decree of a United States Circuit Court, as was held in McNulta *v.* Lochridge, *supra*, then a right of suit thus conferred by congress cannot be restricted in advance of its exercise. This would be, in effect, to nullify the act of congress, and, therefore, in excess of jurisdiction. The power given by the proviso ["but such suit shall be subject to the general equity jurisdiction of the court in which such receiver or manager was appointed, so far as the same shall be necessary to the ends of justice"] must not be so construed as to authorize the courts to prevent that which congress has expressly provided may be done. That it was intended by congress that some meaning should be attached to the very significant proviso [above quoted] is most obvious. It was not intended that the rights to litigate with the receiver in any court should be an unrestrained right. Whether the proviso should be lim-

on the business connected with the property in his charge.[1] The Supreme Court of Minnesota has held that an indebtedness incurred by the receivers of a railway company appointed by the federal court, while operating the road under the authority of the court, may be garnished in a state court. But no executory process can be issued against the receivers on the judgment rendered therein. It can only be satisfied, as other demands are satisfied, by an application to the court in which the receivership proceedings are pending for an order directing its payment.[2] In a case

ited so as to give the court appointing the receiver power upon equitable grounds and upon special application to restrain proceedings in a pending suit brought without leave of the court, or whether, after judgment, the court would exercise its equitable jurisdiction by inquiry into the judgment, in order to determine its justice or its place and rank in the distribution of the property out of which it is to be paid, are questions which need not now be settled. A wide difference of opinion has been entertained as to the power of the court over property obtained against the receiver in courts other than that appointing the receiver. Central Trust Co. *v.* St. Louis, etc., Ry. Co., 40 Fed. Rep. 426; Eddy *v.* Wallace, 49 Fed. Rep. 801; s. c., 1 C. C. A. 435; Missouri Pac. Ry. Co. *v.* Texas Pac. R. Co., 41 Fed. Rep. 311. In the two cases first cited it was held that such judgments were conclusive. In the case reported in 41 Fed. Rep. 311, it was held that it was within the power of the court when such judgments were filed in the case in which the fund was being distributed to look into them and allow the whole or half or any part as justice might require. The latter view seems to have been entertained by Mr. Justice JACKSON, for, while judge of this circuit, he made an order in this cause, which has not been revoked, requiring all judgments in other courts, obtained in suits prosecuted without leave of the court, to be filed by intervening petition in the main cause, together with a full bill of exceptions showing the evidence upon which the judgment rested. That the judgment is conclusive so far as to be regarded as a judicial ascertainment of liability and of the amount is probably the better view. Speaking of the effect of the proviso, the learned chief justice, in the case of Railway Co. *v.* Johnson, *supra*, said that 'the right to sue without resorting to the appointing court, which involves the right to obtain judgment, cannot be assumed to have been rendered practically valueless by this further provision in the same section of the statute which granted it.'"

[1] Central Trust Co. of New York *v.* East Tennessee, V. & G. Ry. Co., (1894) 59 Fed. Rep. 523.

[2] Irwin *v.* McKechnie, (Minn. 1894) 59 N. W. Rep. 987: MITCHELL, J., for the court, said: "No question is made, nor could well be, but that, under the 'Removal Act' of March 3, 1887, the receivers are subject to suit in respect to any transaction of theirs in operating the road, the only point made being that the money sought to be reached was *in custodia legis*, and hence not subject to garnishment. No one will question the correctness of

in the United States Circuit Court for the southern district of Iowa, the receiver of a railroad and its property appointed by that court applied to the court for an order and writ of injunction, with reference to garnishment proceedings about to be brought in the state courts to reach wages of his employees in his hands. The court, while hesitating to attempt a process of injunction which might in any event or to any degree affect actions pending or about to be brought in the courts of the state, did direct its receiver, upon service of notice of garnishment upon him, as receiver, in the state courts, to file with the officer serving the process an uncertified copy of an order made by the court, and thereafter to take no further part, as such receiver, in the action. The order referred to was finally to the effect "that if any plaintiff or claimant in or under said garnishment action, notice, writ or process shall thereafter further proceed therewith in said state court, such plaintiff or claimant shall not be granted leave nor allowed to file in this court any application or claim for payment of or with reference to said claim so set up in said state court or judgment thereon (if any rendered thereon), nor shall he be decreed or permitted to receive therefor from said receiver or through this court, in any manner, any wages or funds that at any time may be in the hands of said receiver, which may be due or belong to any alleged debtor in

the proposition that property in the hands of receivers appointed by the court is *in custodia legis*, and not subject to levy or garnishment. This doctrine receives additional force in this case from the rule of judicial comity between state and federal courts, by which each will refuse to interfere with property in the custody of the other, a rule which we are always solicitous to observe. But in this case it will be noticed that what is sought to be reached by garnishment is the property, not of the railway company, but of the defendant, viz., a debt due from the receivers. Moreover, while garnishment of a debt is often called a mode of attachment, yet it does not effect a specific lien on any property. The effect of the judgment is merely to determine the existence and amount of the debt, and to substitute the plaintiff for the defendant as the person to whom it is payable. The judgment against the receivers would not be against them personally, but against them officially. No executory process could be issued on it, for that would interfere with the control of the property in the custody of the federal court. The manner in which the judgment so rendered shall be paid must be under the exclusive control of that court. It can only be satisfied as other demands may be satisfied, viz., by an application to the court in which the receivership proceedings are pending for an order directing its payment in the due order of the settlement of the affairs of the insolvent company by that court."

such garnishment proceedings, nor the payment of any costs in such proceedings incurred."[1]

§ 554. Claims against receivers for injuries to persons or property during receivership.— Where a railroad was being operated by a receiver, the receiver, and not the railroad company, has been held liable, under the provisions of the Code of Iowa, for the value of stock injured on the railroad company's unfenced right of way through the negligence of the railroad employees. And in such a case the service of notice in due form of a claim for damages for an injury to stock upon the receiver and a station agent in the county where the stock was injured was held sufficient, under that provision of the Code, to entitle the claimant to recover double damages for another injury, if payment was not made within thirty days after the service of such notice.[2] Another action for damages of a similar kind was

[1] In re Barnard; United States Trust Co. of New York *v.* Omaha and St. Louis Ry. Co., (1894) 61 Fed. Rep. 531. It was said by the court, as justifying such an order: "That the bringing of actions in the state courts by creditors of employees engaged in connection with said railway, to be accompanied with garnishment of the receiver, must necessarily be attended with trouble and expense to said receiver cannot be doubted. These actions, it is well known, are generally for small amounts, and are brought mostly before justices of the peace over widespread area and in any county in which, under the statutes of the state, service may be had. They thus become to the receiver a matter of serious inconvenience if not of possible hazard because of the judgments that may be therein rendered. But to our mind there is a consideration of a much more serious nature. The railway company is in the hands of this court. Its employees are in the service of this court. It is the duty of the court through its receiver and employees to maintain and operate said road as efficiently as practicable. The court recognizes that these employees are generally dependent for their living upon the wages contracted to be paid them for their labor upon and in connection with said railway. These garnishment proceedings are instituted for the purpose of collecting debts due to outside creditors, and the motive is to seize and appropriate these wages — the livelihood — of these employees for the payment of such debts. In other words, the wages of the employees of this court necessary for their present living are, in these garnishment proceedings, to be diverted from such use. The effect must be to diminish the power of this court to operate the road. To take away the support of the employees is to cripple the efficiency of such operation, and this court is not powerless to prevent its employees from being starved out of its employ."

[2] Brockert *v.* Central Iowa Ry. Co., (1891) 82 Iowa, 369. Whether in the action the railway company was a proper or necessary party, *quære.* As to the liability of receivers in such actions, see Beach on Receivers. §§ 721–

brought in the Texas courts against a receiver of the railroad property appointed by the United States Circuit Court and the railroad company which finally purchased the property from the purchaser at the sale under the receivership by order of the federal court. There was a judgment against the company, but in favor of the receiver. Upon the appeal of the company to the Court of Civil Appeals of Texas, this latter court held that the federal court, having exclusive jurisdiction of the property and assets of this railroad company, appointed a receiver therefor, and ordered that all claims against the railroad should be by intervention in the receivership proceeding before a certain date, the claim of the plaintiff here having occurred during the receivership, and not having been presented before the federal court within the time allowed, was barred.[1] On the ground that

723 and notes; Ohio & Mississippi Ry. Co. *v.* Davis, 23 Ind. 553; Memphis & L. R. Ry. Co. *v.* Stringfellow, 44 Ark. 322; Stephens *v.* Railroad, 36 Iowa, 327.

[1] Dillingham *v.* Kelley, (Tex. Civ. App. 1894) 27 S. W. Rep. 806. It was said by the court: "Under the general rules of law, as administered in courts of equity, a railroad corporation is not liable for damages sustained by the negligence of a receiver while operating the road except when the road is returned without sale to its owner with improvements made thereon by the receiver out of the earnings of the road while in his possession. If there be a sale of the property under decree of the court the purchaser takes it, together with whatever improvements may have been made by the receiver, free from all charges or burdens except such as may have been imposed by the decree, or such as may have existed prior thereto. In the case of Railway Co. *v.* Johnson, reported in 76 Tex. 421; s. c., 13 S. W. Rep. 463, and in 151 U. S. 81; s. c., 14 Sup. Ct. Rep. 250, and upon which appellee seems to rely, the property of the company was returned to it without sale, with large improvements made thereon by the receiver, and it was held by both the Supreme Court of Texas and the Supreme Court of the United States that a recovery against the defendant company was right; and it is to be noted that in the opinion delivered by each of these courts the fact that there was no sale of the property is emphasized. The Circuit Court in which the receivership was pending had exclusive jurisdiction of the property and assets of the railway company, and while the act of congress of 1887–1888 gives the right to any one aggrieved by a receiver to sue him in another court without first obtaining permission from the court in which the receivership is pending, the act expressly provides that the latter court is not to be deprived of or impeded in the exercise of its equity jurisdiction; and in the proper exercise of its powers the Circuit Court, by appropriate orders and the customary notices, took steps to provide for the payment of all just claims against either the receiver of the road or its property, and required all persons having claims to present the same to that court, within a reasonable time, for adjudication, and to that court the plaintiff should have

it was just and good policy the federal courts have ordered receivers of railways under their control to pay wages of employees injured while employed on their lines of road during recovery from those injuries.[1] The intervener in this case, where a railroad was in the hands of receivers, was a baggagemaster claiming damages for an injury resulting from the negligence of other trainmen under the statutes of Kansas, which provide that "every railroad company organized or doing business in this state shall be liable for all damages done to any employee of such company, in consequence of any negligence of its agents, or by any mismanagement of its engineers or other employees." The United States Circuit Court of Appeals for the eighth circuit held that the right of the intervener under that statute was in no wise affected by the fact that the railroad was at the time in the custody of a receiver, and operated by him.[2] In an action against receivers

applied for compensation for the alleged injury received through the negligence of the receiver. Neither the legislature nor the judiciary of a state can defeat or restrain the federal courts in the legitimate exercise of their jurisdiction. The act of the legislature of Texas of 1889, known as the 'Receivers' Act,' has no application to receivers appointed by the federal courts; and a judgment rendered by a state court against such receiver cannot be executed by the state court, but must be referred for payment to the federal court in which the receivership is pending.' See Fordyce *v.* Du Bose, (Tex.) 26 S. W. Rep. 1050.

[1] Missouri Pac. R. Co. *v.* Texas & Pacific Ry. Co., (1888) 33 Fed. Rep. 701; Missouri Pac. Ry. Co. *v.* Texas & Pacific Ry. Co., (1890) 41 Fed. Rep. 319.

[2] Hornsby *v.* Eddy, (1893) 56 Fed. Rep. 461, following Trust Co. *v.* Thomason, 25 Kans. 1. THAYER, D. J., speaking for the court, said: "It is clear that with respect to persons employed by a railway company as railway operatives the statute * * * changes the rule of the common law that the master is not liable to a servant for an injury sustained in consequence of the negligence of a fellow-servant. Does the fact that a receiver is appointed to temporarily operate a railroad forthwith alter the status of all of its employees, and re-establish as to them the old rule of the common law, so long as the receiver remains in charge? Viewing the question in the light of those circumstances of public policy, which probably gave birth to the statute, we cannot conceive of any reason why the appointment of a receiver should have such effect. It is a fact of which we may well take judicial notice that great railway systems, which employ thousands of men, are frequently operated for a term of years through the agency of a receiver. Such receivers do not, as a general rule, change the working force of the road, or the rules and regulations by which trains are run or by which the other business of the road is transacted. The men whom they employ are engaged in the same *quasi* public service as other railway employees and daily en-

of a railroad company for damages to a crop of hay by fire caused by sparks from the locomotive engine, service was perfected upon the receivers by service upon a station agent in their employ. A motion made to quash the service was overruled and an exception served. Before the United States Circuit Court of Appeals for the eighth circuit it was contended that the lower court, on this state of facts, did not acquire jurisdiction to enter a judgment against the receivers. The Court of Appeals disregarded the contention for two reasons: *Firstly.* The 3d section of the Judiciary Act of March 3, 1887, authorizing suits to be brought against receivers of railroads, without special leave of the court by which they are appointed, was intended, as the court thought, to place receivers upon the same plane with railway companies, both as respects their liability to be sued for acts done while operating a railroad and as respects the mode of obtaining service.[1]

counter the same risks and hazards. Furthermore, the receiver of a railroad operates it for the immediate benefit of the company by which it is owned, in that he discharges all of the public duties of the corporation and appropriates the income of its road to the preservation of its property and franchises, and to the payment of its debts. In view of the fact that many railroads have been operated for years by receivers, and the manner in which it is customary to operate them, congress has recently recognized both the justice and expediency of placing such receivers on a plane with railway corporations, by declaring, in explicit language: 'That whenever in any cause pending in any court of the United States, there shall be a receiver or manager in possession of any property such receiver or manager shall manage and operate such property according to the requirements of the valid laws of the state in which such property shall be situated, in the same manner the owner or possessor thereof would be bound to do if in possession thereof; * * * and that every receiver or manager of any property appointed by any court of the United States may be sued in respect of any act or transaction of his in carrying on the business connected with such property, without the previous leave of the court in which such receiver or manager was appointed.' 24 U. S. Stat. at Large, 554; Eddy *v.* La Fayette, 49 Fed. Rep. 807; s. c., 1 C. C. A. 441. The general constructions warrant the conclusion that, if the rules of the common law are modified for the benefit of the employees of railway companies, either because of the extraordinary dangers to which they are exposed, or the *quasi* public nature of the service in which they are engaged, or for any other reason, then, for like reasons, the old rule of the common law should not be held applicable to the employees of a receiver who is engaged in operating a railroad, and we can scarcely conceive that any legislative body would intentionally make any distinction between the two classes of employees last referred to."

[1] Following and concurring in what was said in Central Trust Co. of New York *v.* St. Louis, A. & T. Ry. Co., (1889) 40 Fed. Rep. 426. CALDWELL, J., said in this case: "This act

Secondly. By answering to the merits and going to trial after the motion to quash the service had been overruled, the receivers submitted to the jurisdiction of the court, and should not be permitted to question its jurisdiction in this court.[1]

§ 555. Rules as to actions for injury to persons during receivership.— The United States Circuit Court for the district of South Carolina refused leave for an action for personal injuries sustained before the appointment of a receiver of a railroad company within its jurisdiction, upon the ground that such an action could not be maintained against the receiver, but must be brought against the corporation.[2] Actions are maintainable against

was intended to correct abuses that had grown up under the old practice, one of which was pointed out before the passage of the act, in the opinion of this court in Dow *v.* Railroad Co., 20 Fed. Rep. 267. The act abrogates the old rule on the subject of suing receivers. It is no longer unlawful to sue a receiver appointed by a United States court without leave of the court appointing the receiver. The court had had no discretion to say when its receiver may be sued. The act gives the right, without condition of qualification. It is a right not to be nullified, evaded or abridged. No conditions can be imposed in its exercise. The court must give effect to the act. It has no discretion to do anything else. * * * The road the receivers are operating under the authority of this court runs clear across the state, a distance of three hundred miles; but the receivers have established their office in St. Louis, Mo.; there they remain, and when sued cannot be found and personally served with process in this state. The right to sue the receivers necessarily carries with it the right to serve the required process to make the suit effectual. This is implied in the act. What is implied in an act is as much a part of it as what is expressed. Process need not be served on the railroad receivers personally. It would be impracticable to do so in many cases. It is impracticable in this case. The receivers, like the railroad company, can operate the road only through their agents, who must always be within the jurisdiction of the courts of the state in which the road is operated. For a court to permit its receivers to remain beyond the jurisdiction of the state courts, and refuse to give effect to service on their agents in the state would effectually preclude the citizens from suing them in the state courts, and would bar a complete nullification of the act of congress."

[1] Eddy *v.* La Fayette, (1892) 49 Fed. Rep. 807.

[2] Finance Co. of Pennsylvania *v.* Charleston, C. & C. R. R. Co., (1891) 46 Fed. Rep. 508; citing Davenport *v.* Railroad Co., 2 Woods, 519; Ex parte Brown, 15 S. C. 523. As to liability of receivers of railroad corporations for injuries to persons during the receivership, see Missouri, K. & T. Ry. Co. of Kansas *v.* Chilton, (Tex. Civ. App. 1894) 27 S. W. Rep. 272. As to what need not to be alleged in a complaint against receivers of a railroad company in an action for damages for injuries occurring while they were in possession, and the effect of the stat-

receivers for injuries to employees while operating the road, under the statutes of states making railroad corporations liable for such.[1] Negligence of a receiver in operating the railroad in his charge, under direction of the court appointing him, creates no liability for which the corporation will be liable.[2]

§ 556. **Rules as to allowances to receivers for counsel and expenses of parties in actions where receivers are appointed — what will be allowed and what not.**— Receivers are officers of the courts, entitled to apply to the court for instruction and advice, and permitted to retain counsel, the fees of which counsel being within the just allowances that may be made by the court. The allowance of counsel fees on behalf of a receiver is made to the receiver and not to the counsel. These allowances to a receiver for counsel are largely discretionary, and appellate courts have generally treated the action of the court in making allowances as presumably correct.[3] The compensation of attorneys for receivers is usually determined according to the circumstance of the particular case, and corresponds with the degree of responsibility and business ability required in the management of the affairs intrusted to them, and the perplexity and difficulty involved in that management.[4] In this foreclosure suit the bill alleged the

utes of Texas as to actions against receivers, see Yoakum *v.* Kroeger, (Tex. Civ. App. 1894) 27 S. W. Rep. 953. In Texas & Pacific Ry. Co. *v.* Gay, (Tex. Civ. App. 1894) 27 S. W. Rep. 742, where the court found that a receiver for a railroad situated wholly within the state of Texas was appointed by a Federal District Court of another state, through the collusion of the railroad company, the Court of Civil Appeals held that the receiver would be treated as the agent of the company, and on the discovery of the fraud the company might be substituted as defendant in an action for the death of plaintiff's husband, originally brought against the receiver, so as to avoid the bar of the Statute of Limitations.

[1] Rouse *v.* Harry, (Kans.) 40 Pac. Rep. 1007; McGhee *v.* Claridy, (Ga.) 22 S. E. Rep. 375.

[2] Howe *v.* St. Clair, (Tex. Civ. App.) 27 S. W. Rep. 800; Memphis & C. R. R. Co. *v.* Hoechner, 67 Fed. Rep. 456; s. c., 14 C. C. A. 469.

[3] Stuart *v.* Boulware, (1890) 133 U. S. 78.

[4] Stuart *v.* Boulware, (1890) 133 U. S. 78. See Trustees *v.* Greenough, 105 U. S. 527, 537, where the subject is considered. Cases declaring rules as to compensation to receivers, expenses of counsel, etc., out of the trust funds in the hands of the court appointing such receivers: Crumlish's Admr. *v.* Shenandoah Valley R. R. Co., (W. Va. 1895) 22 S. E. Rep. 91; Abbott *v.* Packet Co., 4 Md. Ch. 310; Magee *v.* Cowperthwaite, 10 Ala. 966; Gardiner *v.* Tyler, 3 Keyes, 505; Cowdrey *v.* Railroad Co., 1 Woods, 346; s. c., Fed. Cas. No. 3,293; Farmers' Loan & Trust Co. *v.* Central Railroad of Iowa, 8 Fed.

railroad company's insolvency and the insufficiency of its assets to pay the mortgage bonds. The validity of the bonds was contested by the company, and during the litigation the company moved the court to order the receiver to pay certain sums to the company's counsel for services rendered and to be rendered; also, to pay its office expenses and the salary of its secretary, claiming that such payments were absolutely necessary to maintain its corporate existence and enable it to defend. The United States Circuit Court held that as such bonds were *prima facie* valid the holders of the bonds were entitled to all the assets, and to make such payments would be to impair their vested rights.[1] In this foreclosure suit it appeared that the receiver of a railroad employed attorneys, who, after protracted litigation, much reduced the claims of a certain lienholder. Afterwards the property was sold subject to that lien, and the receiver was discharged. The purchasing company recognized the claim of those attorneys for fees, and made a payment on account. There was another receivership afterwards in foreclosure proceedings brought by one claiming under a lien created by the new company, the purchasing company above referred to. Upon a petition of those attorneys in these last proceedings for an allowance of counsel fees the United States Circuit Court for the district of South Carolina held that they had no claim as against the new receiver, or the funds in his hands, as their services had nothing to do with keeping the road a going concern; that the recognition of their claims by the purchasing company amounted to no more than a simple contract which was not entitled to priority to the vested liens created by that company. Neither did the fact that

Rep. 60; Central Trust Co. *v.* Wabash, St. L. & Pac. Ry. Co., 32 Fed. Rep. 187; French *v.* Gifford, 31 Iowa, 428; Stuart *v.* Boulware, 133 U. S. 78; s. c., 10 Sup. Ct. Rep. 242; Tutt *v.* Sand Hills Hotel Co., (Ga. 1894) 22 S. E. Rep. 196. For a case where it was held that it was in the power of the court to render a final decree fixing and allowing the compensation of the receiver, counsel fees and other charges and expenses of administration; that every party to the entire case was bound to take notice of the action of the court, and that it was too late at a subsequent term of the court to except to the decree or move to set it aside for mere error, see Clements *v.* Empire Lumber Co., (Ga. 1895) 22 S. E. Rep. 987.

[1] Union Loan & Trust Co. *v.* Southern California Motor Road Co., (1892) 51 Fed. Rep. 106. Denying the motion, the court cited Beach on Rec. §§ 376, 752, among other authorities as supporting its conclusion.

the services of these attorneys, by reducing the claim of a prior lienholder, incidentally benefited all subsequent lienholders constitute any ground of priority in the absence of any contract of employment by them.[1] The mortgage of a manufacturing corporation had been foreclosed by a decree, and a petition was made therein for allowance of attorney's fees. The trust deed or mortgage given to secure the bonds of the corporation provided for payment of the trustee's expenses upon a sale by him under the powers contained in the deed. The trustee had foreclosed by suit, a course which was probably necessary because of a prior foreclosure sale in the state court. The suit was brought on request of certain bondholders, and the trustee had refused to act except under a stipulation that he should not be liable for the attorney's fees. The United States Circuit Court for the northern district of Georgia on the petition held that the trustee was not entitled as a matter of right to have attorney's fees taxed.[2] A trust company, which has been compelled to come into court to collect from the receiver of a railroad company certain rentals justly due, cannot claim compensation for the services of its solicitors in procuring the order for payment, when such services were entirely for its own benefit, and not for the purpose of saving or adding to the fund which was to be distributed to the creditors in general.[3] There was a contention in this case that

[1] Bound *v.* South Carolina Ry. Co., Ex parte Mitchell, (1892) 51 Fed. Rep. 58. See Hand *v.* Railroad Co., 21 S. C. 162.

[2] Robinson *v.* Alabama & Georgia Manufg. Co., (1892) 51 Fed. Rep. 268, following Fowler *v.* Trust Co., 141 U. S. 384; s. c., 12 Sup. Ct. Rep. 1.

[3] Central Trust Co. of New York *v.* Valley Ry. Co., (1893) 55 Fed. Rep. 903. To support its claim for compensation the trust company relied upon Investment Co. of Philadelphia *v.* Ohio & N. R. Co., 46 Fed. Rep. 696, and Easton *v.* Railroad Co., 40 Fed. Rep. 189. The court distinguished these cases in these words: "In both these cases the party claiming compensation from the court was a trustee named in the mortgage foreclosed, upon whom, by virtue of that contract relation, certain duties devolved connected with the mortgages. In the [first case] the trustee, having declined to proceed with a suit of foreclosure, and that duty having devolved upon the complainant for himself and other bondholders, the court disallowed the claim of the trustee for compensation, but did allow compensation for the complainant; the trustee in that case had been made a defendant and his duties were merely nominal. No active service in his behalf was performed in executing the trust and bringing the fund into court available for distribution to the beneficiaries under the mortgage. In the [second case] compensation was allowed the trustees of the several mortgages in

the receivers ought to have no say in the matter, because the claim was one which the receivers recognized to be just, as rentals for cars which they had in their possession and actual use, and because the receivers did not move in these proceedings, and the trust company was compelled to do so; therefore, counsel fees were due to it out of the fund to arise in the case. But the court held that it was not the duty of the receivers to proceed affirmatively and procure the allowance of every claim preferred against them.[1]

§ 557. **Actions allowed a receiver for the protection and benefit of the property in his hands.**—These rules were declared in a foreclosure suit against a railroad company in the United States Circuit Court for the district of South Carolina. A federal court has power to enjoin a sheriff from distraining property in the hands of its receiver to enforce the payment of a tax which is alleged to be illegal, especially where the property seized many times exceeds in value the amount of the tax. The mere fact that under the state statute authorizing sheriffs to distrain for non-payment of taxes "sufficient personal property of the party charged" to pay the tax, a sheriff, in order to collect a tax of $1,200, alleged to be due from the railroad receiver, had distrained property worth $10,000, much of which belonged to third persons, was held sufficient to require the interference by injunction of the court which appointed the receiver, regardless of any question as to the validity of the tax. While property in the hands of a receiver of a federal court is bound for the payment of state taxes in the same manner as any other property, still, should the receiver believe the tax to be invalid, it is his right and duty to apply to the court appointing him for pro-

that case because it appeared from the report of the master, as reviewed by the court, that active duties had devolved upon those trustees, and that by virtue of their relation to the mortgage compensation was justly due them."

[1] Central Trust Co. of New York *v.* Valley Ry. Co., (1893) 55 Fed. Rep. 903. It was said: "The receivers are the officers of the court, and the order appointing them states generally the nature of the claims which they are authorized to pay. The claim represented in the motion now under consideration was one which required the issuing of receivers' certificates, and for which affirmative action on the part of some one was necessary. It was no part of the receivers' duty to move affirmatively in this matter, but it is the duty of the creditor so to do. The same duty devolves upon every creditor having a claim against this insolvent railroad."

tection. And where, in his application to the court in such case for protection, his action is based on a prior decision of the court appointing him that the tax was illegal, the court should extend such protection by enjoining the sheriff and requiring the property to be restored to the receiver until the presumption of the soundness of such prior decision has been overcome.[1] The United States Circuit Court for the district of South Carolina entertained jurisdiction of a proceeding by receivers of a railroad company against the state railroad commissioners for relief against alleged unjust and unreasonable rates for freight transportation established by the commissioners over the objection that it was a proceeding against the state within the eleventh amendment to the Constitution of the United States, inhibiting the exercise of jurisdiction by federal courts in suits brought against one of the United States by citizens of another state.[2] The bill filed

[1] Ex parte Chamberlain, (1893) 55 Fed. Rep. 704. It was said in the opinion: "The research of counsel on both sides of this case has succeeded in finding five cases in which a receiver was driven to seek the protection of the court in the matter of taxation; all of them of persuasive authority; more of them of conclusive authority. A petition was filed by a receiver before Judge BREWER in Central Trust Co. *v.* Wabash, St. L. & P. Ry. Co., 26 Fed. Rep. 11, praying protection from the payment of a tax. It appeared that the only reason for the application was that it was inconvenient to the receiver to pay the tax, and that its validity was in no way questioned. The petition was rejected. But the learned judge shows distinctly his opinion that upon proper showing he would have entertained the petition. This is his language: 'In levying and collecting taxes the state is exercising its sovereign power. There should be no interference with its collection of these taxes in its prescribed and regular methods, even by a court having property in the possession of its receiver, unless it is first charged that the taxes are in some way illegal or excessive.' A bill was filed in Hewitt *v.* Railroad Co., 12 Blatchf. 452, by receivers to test the legality of a tax. It was heard by Mr. Justice BLATCHFORD, who entertained the question, discussed it in a long and elaborate opinion, and sustained the legality of the tax. The same receivers came before him again in Stevens *v.* Railroad Co., 13 Blatchf. 104, and asked relief from the same tax, because of some irregularity. Naturally and properly, it having been decided that the tax was legal, he dismissed the petition. As we have said, a receiver must pay all legal taxes, and the court will not interfere to protect him if he attempt to escape from such payment. In Georgia *v.* Atlantic & G. R. Co., 3 Woods, 437, Mr. Justice BRADLEY did interfere with the summary process of collecting taxes by the state, and in his well-considered and able opinion established the right of interference upon the highest grounds of public policy."

[2] Clyde *v.* Richmond & Danville R. Co., (1893) 57 Fed. Rep. 436. SIMONTON, D. J., said: "This case presents no question of penalties. The state is in no sense a party to the record or

here by the receiver of a railroad company's property in a foreclosure suit to have certain leases of property of the railroad company which had been assigned to defendants declared void, based on allegations that this property which was land belonging to the railroad company had been leased to a director of the company who held nearly all its stock, which had been assented to or ratified by the other directors, who held nearly all of its remaining stock, was dismissed, the federal court holding that the receiver could not contest the validity of the leases, he not representing creditors and no circumstances being alleged vesting in him equities to maintain such a suit or to question the lessee's rights.[1]

privy to the record. The constitutionality of the statute under which respondents act is not in issue. The learned counsel for the state admit that the declaration of this statute that the rates fixed by the commission shall be sufficient evidence that they are just and reasonable, does not preclude the courts from examining into the fact whether they are just and reasonable. Under the statute the respondents are authorized and directed to make just and reasonable rates for the transportation of freight. The petition alleges that certain rates made by them are neither just nor reasonable. In this issue the sovereignty of the state is in no way involved." See Railway Co. *v.* Dey, 35 Fed. Rep. 873.

[1] Tyler *v.* Hamilton, (1894) 62 Fed. Rep. 187.

CHAPTER XXX.

PRIORITIES OF LIENS IN FORECLOSURE SUITS.

§ 558. Priorities of liens — general rules.
559. Debts contracted for construction.
560. Presumption as to preferential character of a claim.
561. Mechanic's lien as viewed by the United States Supreme Court.
562. Furnishers of supplies — Kentucky statutes construed,
563. The rule under Ohio statutes.
§ 564. Contractors — Tennessee statutes construed.
565. Furnishers of supplies — Virginia statutes on this subject construed.
566. Loans of money to corporation before receivership.
567. Claims for services rendered the corporation prior to the appointment of a receiver.
568. When cases are not properly removable to United States court from state court.

§ 558. Priorities of liens — general rules.— As a rule, statutory liens should be paid out of the proceeds of sale of mortgaged property before mortgage bonds and equitable liens payable from earnings after such bonds.[1] The claim of an owner of land for damages, resulting from the construction and maintenance on a street in front of his land of a railroad mounted on trestle work, has been held superior to the claims of mortgage bondholders.[2] It has been held that persons conveying a right of way in the state of Tennessee directly to a railroad company have a lien for the purchase price prior to that of the mortgage bonds of the railroad company.[3] A railroad company, after mortgaging its real estate, purchased from interveners rolling stock, to be paid for in installments, the vendors securing title in themselves until paid for. A receiver was appointed in a judgment creditor's suit, the mortgagees not objecting. The latter afterwards brought

[1] Blair *v.* St. Louis, Hannibal, etc., R. R. Co., 25 Fed. Rep. 232.

[2] Mercantile Trust Co. *v.* Pittsburgh & W. R. Co., 29 Fed. Rep. 734. A case holding certain equipment bonds of a railroad company, afterwards consolidated with other companies, to have priority to consolidated mortgage bonds, under the Ohio statutes, see Compton *v.* Wabash, St. L. & P. Ry. Co., (Ohio) 16 N. E. Rep. 110. When outstanding debts of one of the constituent companies consolidating should have priority over the debt secured by first mortgage bonds, see Spence *v.* Mobile & Montgomery Ry. Co., 79 Ala. 576. That a receiver's expenditures may be made a preferred claim, see Hale *v.* Nashua & Lowell R. R. Co., 60 N. H. 333.

[3] Central Trust Co. of New York *v.* Bridges, (1893) 57 Fed. Rep. 753.

suit to foreclose their mortgage. Before a decree, the cars were returned to the vendors. The United States Supreme Court held that the first receiver not having been appointed at the instance of the mortgagees, the vendors of the rolling stock were not entitled to have their claim for rental of the rolling stock during the first receivership paid in preference to the mortgage debt out of the proceeds of the real estate sold under the mortgage foreclosure. But they were entitled to have their rental, after the commencement of the mortgagees' foreclosure suit, paid in preference to the mortgage debt, the receiver having retained possession of it and used it for the benefit of the property mortgaged.[1] A priority of lien to the mortgage was claimed in a Virginia case of certain "car trust claims," under a statute of that state, which statute the Supreme Court of Appeals held to be unconstitutional as to that part of it including the furnishing of cars and engines to a railroad company. It was insisted before the court that, though the statute was invalid, the claims in question were privileged debts, entitling the claimants to superior equities to the mortgage creditors, according to the doctrine well established in this country that, when the current receipts of a railroad, which are always first applicable to the payment of its current debts, *i. e.*, debts for labor, supplies and the like, are used in paying the mortgage debt, or in strengthening or protecting the security, it is competent and proper for a court of equity, when asked by the mortgagees to take possession of the road, and to hold and operate it for their benefit by the appointment of a receiver, to direct that the fund thus diverted be restored from the income of the receivership, or, under some circumstances, even from the proceeds of the sale of the *corpus* of the other property.[2] The court held that these "car trust claims" were not within the principles of the cases referred to, and were not entitled to any priority of lien to the mortgage.[3] The United States Supreme Court reversed the Circuit Court in this case, and

[1] Kneeland *v.* American Loan & Trust Co., 136 U. S. 89; s. c., 10 Sup. Ct. Rep. 950.

[2] See as to this doctrine, Fosdick *v.* Schall, 99 U. S. 235; Union Trust Co. *v.* Souther, 107 U. S. 591; Burnham *v.* Bowen, 111 U. S. 776; St. Louis, etc., R. R. Co. *v.* Cleveland, etc., Ry. Co., 125 U. S. 658, 673; Hale *v.* Frost, 99 U. S. 389; Williamson *v.* Washington City, Virginia Midland & Great Southern R. R. Co., 33 Gratt. 624.

[3] Fidelity Insurance Trust & Safe Deposit Co. *v.* Shenandoah Valley R. R. Co., (1889) 86 Va. 1.

held that a debt due from a railroad company to a car company for rental of cars prior to the commencement of the suit to foreclose a mortgage on the road and the appointment of a receiver was not a preferred debt, having priority over the mortgage debt.[1] In this case, the Supreme Court also reversed the court below in its allowance of interest on a claim for car rentals.[2] Where notes were given for money borrowed to pay interest on the bonded debt, with a stipulation in each note that a certain amount of the gross earnings of the road, from the date of the note, "is pledged in liquidation of this note," it has been held that the effect of the stipulation being ineffectual, these notes were not entitled to any priority of lien to the mortgage. But debts incurred by the company, within six months before the receivership, for construction of new road were held entitled to payment out of the net earnings of the receivership, in preference to mortgages executed before the road was finished, and showing

[1] Thomas *v.* Western Car Co., (1893) 149 U. S. 95, reversing Thomas *v.* Peoria & R. I. Ry. Co. (Western Car Co., Intervener), (1888) 36 Fed. Rep. 808. Mr. Justice SHIRAS, speaking for the court, after quoting largely from Miltenberger *v.* Logansport Ry., 106 U. S. 286, and Kneeland *v.* American Loan Co., 136 U. S. 89, 97, said: "Tested by the principles asserted in these cases, the claim for car rental that had accrued prior to the receivership cannot be maintained. but should have been disallowed. The case of a corporation for the manufacture and sale of cars, dealing with a railroad company, whose road is subject to a mortgage securing outstanding bonds, is very different from that of workmen and employees, or of those who furnish from day to day supplies necessary for the maintenance of the railroad. Such a company must be regarded as contracting upon the responsibility of the railroad company, and not in reliance upon the interposition of a court of equity. In the present case it appears, in the contract between the car company and the railroad company, that the former reserved the express right to terminate the contract and demand possession of the cars forthwith upon any failure by the railroad company to promptly pay the interest or the principal of any of its bonds or other liabilities. Such a provision shows that the car company was aware of the existence of the outstanding bonds, and protected itself by other methods than relying upon the possible order of a court which might appoint a receiver. Moreover, it appears in this case that the principal officers of the car company were in control of the railroad company and its operations, and must be treated as having full notice of the financial conditions of the railroad company, and as having leased the cars to it in reliance upon its general credit, rather than in expectation of displacing the priority of the mortgage liens."

[2] Thomas *v.* Western Car Co., (1893) 149 U. S. 95. They said: "As a general rule, after property of an insolvent passes into the hands of a receiver or of an assignee in insolvency, interest is not allowed on the claims against

that it was contemplated that the road should be completed, and that the mortgages attached to the road as fast as completed.[1] It appeared in a foreclosure proceeding and interventions that a railroad company had purchased on a credit of eight months certain rails for its use, promising to pay for them out of its earnings. Only a part of the purchase money was paid at the end of the eight months, the notes for the balance being extended. Before the expiration of the credit thus extended the company had paid interest on certain mortgage bonds, borrowing the money for the purpose on its notes, which were afterwards paid out of its earnings. The receiver in this case was appointed eighteen months after the purchase of the rails. The holders of these notes given for the purchase of the rails claiming a priority to the mortgage out of the proceeds of the sale on foreclosure, it was held by the United States appellate court that the giving of the credit by the sellers of the rails to the company indicating an expectation that the interest on the bonds becoming due in the meantime would be paid, the payment of this interest was not a diversion of earnings within the rule giving a preference, on foreclosure, to current expenses incurred on the faith of earnings shortly before the appointment of a receiver.[2] The United States Supreme Court has held that a liquidated claim against a railroad company, not converted into a judgment, which another railroad company, purchasing its road and property, agreed with the selling company to assume and pay as part of the consideration, did not thereby become a lien upon the property so as to

the funds. The delay in distribution is the act of the law; it is a necessary incident to the settlement of the estate. Williams *v.* American Bank, 4 Met. 317, 323; Thomas *v.* Minot, 10 Gray, 263. We see no reason in departing from this rule in a case like the present, where such a claim would be paid out of moneys that fall far short of paying the mortgage debt."

[1] McIlhenny *v.* Binz, (Tex.) 13 S. W. Rep. 655.

[2] Bound *v.* South Carolina Ry. Co., (1893) 58 Fed. Rep. 473. An illustration of where there was not such a diversion of earnings of a railroad from the operating expenses as not to give a preference for certain operating expenses over the bondholders out of the proceeds of a foreclosure sale: St. Louis, A. & T. H. R. Co. *v.* Cleveland, C. & C. I. Ry. Co., 8 Sup. Ct. Rep. 1011, following Railroad Co. *v.* Railroad Co., 6 Sup. Ct. Rep. 1094. In Porter *v.* Pittsburg Bessemer Steel Co., (1887) 120 U. S. 649, unsecured floating debts, due by the railroad company for construction, were, in the absence of statutory provision, held not to be a lien on the railroad superior to the lien of a valid mortgage on it, duly recorded, and of bonds secured thereby, and held by *bona fide* purchasers for value.

take priority over the lien of a mortgage made by the purchasing company to secure an issue of bonds.[1] These facts appeared in a case before the United States Circuit Court of Appeals for the sixth circuit: Under the authority of the Michigan statute a railroad corporation sold all its property and franchises to another corporation and this latter mortgaged the same to secure an issue of bonds. A minority stockholder in the former corporation, who had dissented on the question of selling, brought an action against both of the corporations to set it aside, in which action a decree was made upholding the sale, but providing that this minority stockholder, on tendering his stock to the purchasing company, should have a right to receive an equal number of shares in the latter, or to have an execution against the corporation for the value of his stock. He elected to have the execution, and asked that it be declared a prior lien to the mortgage, but this the court denied him. In a suit brought subsequently to foreclose the mortgage executed by the purchasing corporation, he intervened, claiming an equitable lien prior to the mortgage for the value of his stock. The Court of Appeals held that the effect of the decree in his action to set aside the sale was to convert him from a stockholder in the selling corporation to a judgment creditor of the purchasing corporation, and that he had no lien as claimed.[2] In a case in a federal court it was held that a diversion by a railroad company of a fixed sum from the payment of claims for material used in keeping the road a going concern, to the permanent improvement of the road, or to the payment of interest on the bonds, must be made good by the bondholders, and the bondholders consented to make it good by the issue of receivers' certificates and the application of the proceeds to the claims. The materials here were held to be entitled to no further preference from the proceeds of the sale.[3] There having been a foreclosure sale in this case, and the property purchased by a committee of bondholders under a reorganization agreement, upon a distribution of the funds actually in court arising from such sale becoming necessary, there were various interesting rulings upon the various claims to this fund set up by the differ-

[1] Fogg *v.* Blair, (1880) 133 U. S. 534.

[2] Farmers' Loan & Trust Co. *v.* Toledo & S. H. R. Co., (1893) 54 Fed. Rep. 759.

[3] Finance Co. of Pennsylvania *v.* Charleston, C. & C. R. Co. (Pocahontas Coal Co., Intervener), (1892) 52 Fed. Rep. 524.

ent claimants. It was held upon its appearing that there might be claimants against the old company to an amount more than there was in the registry of the court, that the reorganization committee to whom a cash sale of the road was made and confirmed, and who failed to make good their bid, not for want of funds, but because they thought the price too high, could not be excused, on a resale of the property for a less price, from making good the difference, if the unsecured creditors would be benefited thereby. This reorganization committee, having in its hands a surplus of the bonds of one division of this company after paying in bonds the amount of the bid on that road, set up a claim that they were entitled to share in the distribution. Upon this claim it was held that when a reorganization agreement, to which all the bondholders and stockholders of the mortgagor company were parties, plainly showed an intention that the new securities to be issued after the purchase of the road at judicial sale should extinguish the old bonds for which they were to be exchanged, the consummation of the plan of reorganization operated as a payment of the old bonds, and the former holders of those bonds had no claim upon the proceeds of the sale, on the theory that they were to be regarded as unsecured creditors to the amount by which the sum realized fell below the amount of those bonds. Certain judgment creditors, whose original claims were for money advanced previously to the railroad company, having been included in the reorganization agreement on the same basis as the bondholders, were held to be in like position to the bondholders after the completion of the scheme by the delivery of the road to the new company as reorganized, and their claims were also to be considered as paid.[1] This reorganized railroad company had purchased and received possession of the road, and thereafter paid certain taxes and indebtedness incurred by the receiver in the foreclosure suit, without special authority from the court. Such payments, it was held, could not be regarded as loans to the receiver, to be reimbursed from the proceeds of the sale. The court further held that when, by the conditions of a railroad foreclosure sale, the court had required the payment in cash of an amount which was sufficient to meet all the allowed claims and

[14] Central Trust Co. of New York *v.* Cincinnati, J. & M. Ry. Co., (1892) 58 Fed. Rep. 500.

the expenses of the suit (the balance of the sale price being paid in bonds), the subsequent application, by consent of all parties, of part of the money paid in to liabilities not properly chargeable against it, amounted to a waiver by the owners of the allowed claims of their rights, to the extent that such an appropriation of the money reduced the ability of the fund to discharge their entire claims, with interest, and they could not afterwards require the purchasers to substitute sufficient cash in lieu of bonds to pay claims in full. And the receiver in this case, who resided at a distance from the property, and committed the active management of the railroad business to others, was not entitled to the full compensation usually paid to railroad presidents and receivers who are active executive heads of going railroads. He was allowed $2,500 per annum.[1] A claim against a railroad company for causing the death of plaintiff's intestate has been held to be a demand arising from a failure of duty, and one that could not, by its creation, benefit, preserve or increase the *corpus* of the estate of the company, and, therefore, not to be entitled to priority upon the foreclosure of a mortgage executed by such railroad company.[2] The owners of long-time railroad bonds, the company issuing them being solvent and having secured the bonds by mortgage of all its property, and promptly met all its coupons, guaranteed as to the principal and interest by a manufacturing corporation which subsequently went into the hands of a receiver, it has been held, could not prove the guaranty of the insolvent corporation and have a dividend declared thereon, or have money retained in court to meet a possible future liability on the guaranty, as against creditors of the insolvent corporation, who were pressing for a sale and distribution and who held either specific and general liens or demands past due.[1] The property of this railroad company had been sold under foreclosure proceed-

[1] Ibid.

[2] Farmers' Loan & Trust Co. *v.* Green Bay, W. & St. P. Ry. Co. (Franck, Intervener), (1891) 45 Fed. Rep. 664.

[3] Gay Manfg. Co. *v.* Gittings, (1892) 53 Fed. Rep. 45. When arrears of salary of a president of insolvent corporation will not have precedence in payment to a first mortgage deed out of the proceeds of a sale of the property, see National Bank of Augusta *v.* Carolina, K. & W. R. R. Co., 63 Fed. Rep. 25. When a receiver's right to reimbursement for improvements of the roadbed of a mortgaged road is subordinate to the mortgage lien, see Phinizy *v.* Augusta & Knoxville R. R. Co., 62 Fed. Rep. 771; Virginia Development Co. *v.* Crozer Iron Co., (Va.) 17 S. E. Rep. 806.

ings and the proceeds of the sale were in court for distribution. One having a judgment obtained in a North Carolina court against the railroad company for injuries inflicted upon him, claimed priority to the bondholders in the distribution. His action had not been brought within sixty days after the mortgage was recorded. The Code of North Carolina, section 685, referring to corporations, provides as follows: "But any conveyance of its property, whether absolutely or upon condition, in trust, or by way of mortgage executed by any corporation, shall be void and of no effect as to the creditors of said corporation, existing prior to, or at the time of, the execution of said deed, and as to torts committed by such corporation, its agents or employees, prior to, or at the time of, the execution of said deed; provided, said creditors or persons injured, or their representatives, shall commence proceedings or actions to enforce their claims against said corporation within sixty days after their registration of said deed, as required by law." It was insisted that this section of the Code governed the case and that the judgment could not be given preference by reason of the action not having been brought within sixty days. The court, however, ordered that the claim be given priority to the bondholders, holding that the claim was protected by the Code of North Carolina, section 1285, which declares: "Mortgages of incorporate companies upon the property or earnings, whether on bonds or otherwise, hereafter issued, shall not have power to exempt the property or earnings of such incorporations from execution for the satisfaction of any judgment obtained in courts of the state against such incorporation for labor performed, nor for material furnished such incorporation, nor for torts committed by such incorporation, its agents or employees, whereby any person is killed or any person or property injured, any clause or clauses in such mortgage to the contrary notwithstanding."[1]

[1] Finance Co. of Pennsylvania *v.* Charleston, C. & C. R. Co., Ex parte Hudson, (1894) 61 Fed. Rep. 369; affirmed by U. S. Circuit Court of Appeals in Finance Co. of Pennsylvania *v.* Charleston C. & C. R. R. Co., 62 Fed. Rep. 205. SIMONTON, Circuit Judge, said: "The provisions of section 1255 manifestly recognize that equity which, in the decisions of the Supreme Court, underlies Fosdick *v.* Schall, 99 U. S. 235, and the cases following it. Whoever contributes to keep a corporation a going concern by materials or labor must be provided for before mortgage creditors can claim out of the earnings; and so, also, all expenses incident to the keeping it a going concern, including in the expenses all damages for injuries done to life, per-

§ 559. **Debts contracted for construction.**—A debt contracted for "construction" is not entitled to a priority of payment, in proceedings for the foreclosure of a mortgage of the property of a railroad corporation, which is recognized in Fosdick *v.* Schall, 99 U. S. 235, as the equitable right in some cases of a creditor for "operating expenses."[1] The United States Circuit Court of Appeals for the fifth circuit held that, upon the sale of this railroad on foreclosure, it was error to direct payment of claims for supplies furnished prior to the receivership out of the purchase money, no provision for such payment having been made when the receiver was appointed, and there being no evidence that current earnings, before or after the appointment of the receiver, were diverted to the payment of interest on the bonded debt.[2]

§ 560. **Presumption as to preferential character of a claim**—In this action for foreclosure of a railroad mortgage, the Circuit Court allowed an intervening claim based on a judgment recovered in a state court, and directed its payment out of the proceeds of sale. The decree in the case recited that it was one of those claims theretofore adjudged to be of a preferential character. This adjudication as to its preferential character was not appealed from, and the appeal from the decree allowing its payment, the nature of the demand on which the judgment was recovered, was not disclosed by the record. The United States Court of Appeals for the eighth circuit held that it must be pre-

son or property in keeping up this life of the company, enjoying the same preference." Frazier *v.* East Tenn., Va. & Ga. R. R. Co., 88 Tenn. 138; s. c., 12 S. W. Rep. 537.

[1] Mr. Justice LAMAR in Wood *v.* Guarantee Trust & Safe Deposit Co., (1888) 128 U. S. 416; s. c., 9 Sup. Ct. Rep. 131.

[2] Cutting *v.* Tavares O. & A. R. Co., (Florida Central & P. R. Co., Interveners), (1894) 61 Fed. Rep. 150. In American Loan & Trust Co. *v.* East & West R. R. Co. of Ala., (Jersey City Iron Co., Intervener), (1891) 46 Fed. Rep. 101, it was held that a debt created for materials for original construction of a portion of a railroad more than six months before the appointment of a receiver in proceedings for the foreclosure of a mortgage was not within the rule authorizing the court to provide for arrears due for operating expenses of the road out of the net income of the property, and, in the absence of a showing that there had been such a diversion of current funds or income which should have been applied to the payment of the claim for such materials, would not be given a priority over the rights of the mortgage creditors.

sumed that the finding of the lower court as to the character of the claim was correct, and then affirmed the decree allowing it.[1]

§ 561. Mechanic's lien as viewed by the United States Supreme Court.—The trust company which had accepted the trust created in this railroad mortgage and certified the bonds issued under the mortgage, which were sold on the market, upon a default, brought action to foreclose the mortgage. There being a conflict between the interests of the bondholders under this mortgage and the bondholders under another affecting some of the properties, a committee of the bondholders were made parties co-complainants with the trust company. A question was made by an intervener as to whether his claimed mechanic's lien was not a lien prior and preferable to that of the mortgage. Subsequently to the execution of the mortgage he had contracted with the railroad company to build a dock on a river in one of the termini of the roads, a city in Ohio. He had built the dock, received only partial payment, and filed his mechanic's lien for the balance. The lot in which the dock was built was a part of the railroad property covered by this mortgage. The Supreme Court of the United States reversed the Circuit Court's decree in favor of the holder of the mechanic's lien giving him a priority, holding that a recorded mortgage, given by a railroad company on its roadbed and other property, created a lien the priority of which could not be displaced thereafter either directly by a mortgage given by the company or indirectly by a contract between the company and a third party for the erection of buildings or other works of original construction.[2] The master who reported upon the intervening petition of the holder of the mechanic's lien based his award of priority in this case upon the ground of an equitable right arising from the construction of the dock and consequent improvement of the railroad property. The Supreme Court of the United States held that those facts did not give the intervener an equitable lien prior in right to the lien of the mortgage, or furnish equitable reasons why the legal priority belonging to the mortgage should be displaced.[3] It was urged in behalf of the holder of the mechanic's lien in this case upon the

[1] St. Louis S. W. Ry. Co. *v.* Graham, Intervener, (1893) 56 Fed. Rep. 258, following Railway Co. *v.* Stark, 55 Fed. Rep. 758.

[2] Toledo, Delphos & Burlington R. R. Co. *v.* Hamilton. (1890) 134 U. S. 296.

[3] Ibid.

railroad property, in objection to the force of the propositions of law adverse to his claim of right of priority over the mortgage, as applied to the facts here, that at the time this mechanic's lien was created the legal title was not in the railroad company, but in a third party; that as the mortgagor, the railroad company, had no legal title the mortgage given by it created no legal lien; that while by the decree of foreclosure the legal title was transferred to the mortgagor, it was transferred subject to the burden of the mechanic's lien. The Supreme Court did not regard this contention of the appellee, as it appeared from the testimony and the decree that only the naked or legal title remained in this third party, the full equitable title being in the railroad company, and in that company before the contracts were entered into. They said: "The railroad company had the same title when it made the contracts that it had when the work was done and the decree rendered. Hamilton's contracts were with the railroad company, and of course gave a lien upon the lands only to the extent of the title that the railroad company had."[1]

[1] Toledo, Delphos & Burlington R. R. Co. *v.* Hamilton, (1890) 134 U. S. 296. The court distinguished, as showing a different state of facts from that in the case at bar, Williamson, Trustee, *v.* New Jersey Southern Railroad, 28 N. J. Eq. 277, and 29 N. J. Eq. 311, one of the cases especially relied upon to sustain the contention stated in the text, thus: "In [that case] the defendant railroad company had executed a mortgage with the 'after-acquired property' clause in it, duly recorded. It was also the owner of a large majority of the stock in the Long Branch and Sea Shore Company, and was in possession of and operating the latter company's road. No consolidation in fact of the two companies had taken place, but, being in possession of the latter company's road, it had contracted for the building of certain docks, walls and piers at the terminus of such road. Having failed to make payment for such work, a mechanic's lien was perfected upon the latter company's road. Upon a suit to foreclose the mortgage given by the defendant railroad company, the chancellor, laying hold of the fact that the defendant railroad company was the owner of the large majority of the stock — was in possession of and operating the latter company's road — decreed that such road, with its property and franchises, belonged to the defendant railroad company, and as after-acquired property was subject to complainant's mortgage, but subordinate to the mechanic's lien. On review in the Court of Errors and Appeals, as reported in 29 N. J. Eq. [311], the decision of the chancellor was sustained, the court saying: 'Until that decree was signed, the right of the complainant in the lands of the Sea Shore Company under his mortgage was a mere unexecuted equity to have the benefit of such equities as his mortgagor had in the premises, without any legal title in himself or in his mortgagor upon

§ 562. **Furnishers of supplies — Kentucky statutes construed.** — In this intervention in a foreclosure suit it was held that one who furnished labor and materials for the construction of this railroad, under a contract with a sub-contractor, was not embraced within the provision of the Kentucky statute, that persons furnishing labor or materials for the construction of railroads and other improvements "by contract, express or implied, with the owner or owners thereof, or by sub-contract thereunder, shall have a lien thereon" for the price of such labor and materials.[1] It was also held in the same case that the language, "all

which his mortgage, as a consequence, could operate. * * * When the decree of the chancellor was signed, which established the lien of complainant's mortgage on the property of the Long Branch and Sea Shore Company, Berthoud & Co. had, by force of the provisions of the Mechanics' Lien Act, acquired a lien on the premises which related back to the commencement of the building, and was entitled to priority over all conveyances, mortgages or incumbrances subsequent thereto. This lien was not displaced by the chancellor's decree, which, in the absence of fraud, could be effective only to bring under the complainant's mortgage the lands of the Sea Shore Company, subject to such liens as were lawfully acquired while the legal estate was in that company. The chancellor's decree adjudging the validity and priority of the claim of Berthoud & Co. should be affirmed.' Unquestionably such ruling was correct. The owner of a majority of the stock in a railroad corporation has no title to the road. The title is in the corporation, and he is not the corporation. A mortgage by the owner of such stock is no lien upon the road, and does not prevent the casting of any legal lien upon it. So that while, for the many equitable reasons stated in the opinion, the decree vested the property in the latter road in the defendant railroad company, yet it perfected and transferred that title subject to all legal liens then existing upon it. As the Court of Errors and Appeals well said, until that decree was signed the right of the complainant, the mortgagee, was a mere unexecuted equity to have the benefit of such equities as his mortgagor had in the premises." A Connecticut case, Botsford *v.* New Haven, Middletown, etc., R. R. Co., 41 Conn. 454, also relied upon, was similarly distinguished by the Supreme Court as to the facts in these words: "After giving the mortgage the railroad company desired to erect a depot on land adjoining its track. The owner agreed to give the company the land provided it would build a depot. Upon the building a mechanic's lien was filed. The owner had never made a conveyance. Upon a foreclosure of the mortgage the mechanic's lien upon the building and the ground upon which it was constructed was held prior to the mortgage. The decision was based upon the ground that the full equitable title never passed to the railroad company until the completion of the building, and then passed subject to the burden of the mechanic's lien. Hence, though after-acquired property, and subject to the lien of the mortgage, it was, when acquired, already burdened with a lien."

[1] Central Trust Co. *v.* Richmond, N. I. & B. R. Co. (1892) 54 Fed. Rep.

persons who perform labor or furnish labor," did not intend only those only who performed manual labor; and the words would embrace the services of a civil engineer who actually superin-

723. It was said by the court: "The decisions in the different states are in seeming conflict [upon this point], and it is unnecessary to review all of them, as each state has its own peculiar law and state policy. In some of the states it seems to be the policy to create the lien without regard to any contractual relation with the owner of the building or structure, and in other states to confine the lien to those who have contractual relations, directly or indirectly, with the owners of the building or structure, and, in some others, to combine the two by having regard to the contractual relations of the parties, by limiting the persons who, beside the owners, can create a contractual relation under which a lien can be created under the statute. The late Railroad Law of Wisconsin, and also that of Indiana, seems to be of the first class mentioned above. See Mundt *v.* Railroad Co., 31 Wis. 454; also, Redmond *v.* Railway Co., 39 Wis. 426; Colter *v.* Frese, 45 Ind. 97. The laws of other states are to the same effect. The statute of New Hampshire, as construed by the courts of that state, seems to be of the second class. See Jacobs *v.* Knapp, 50 N. H. 71. The [Kentucky] act of 1888, as we construe it, is of the third class, as are also the lien laws of Pennsylvania, West Virginia, Illinois, and the Mechanic Law of Wisconsin. In Harlan *v.* Rand, 27 Pa. St. 514, the court, after stating the great inconvenience of an indefinite extension of the liens under the construction of the statute contended for by counsel, asked, 'What, then, is the limit of these lien rights?' and said: 'We must look to the law for an answer, and we find it in the twelfth section. It distributes all the parties into three classes, according to their several functions: *First*, the owner; *second*, the contractor — called, also, architect and 'builder;' and, *third*, the workmen and materialmen. The law establishes one link, and only one link, between the owner, on the one hand, and the workmen and materialmen on the other. It requires the lien to be founded on contract, and it recognizes no one as having power to contract so as to make a lien against the building, except the owner and the contractor or architect.' Page 576. The West Virginia statutes provide that any mechanic, etc., who performs work or furnishes materials 'by virtue of any contract with the owner thereof, or his agents, or any person who, in pursuance of an agreement with any such contractor, shall, in conformity with the terms of the contract with such owners or agents, do or perform any labor or work, or furnish any material, in the erection or construction of a house,' etc., shall have a lien thereon. In McGugin *v.* Railway Co., 33 W. Va. 67; s. c., 10 S. E. Rep. 36, the court held a contractor once removed from the original contractor, had no lien under this statute. In Illinois the Lien Law of 1869 provided that: 'Every sub-contractor, mechanic, workman, or other person who shall hereafter, in pursuance of the purposes of the original contract between the owner of any lot or piece of ground, or his agent, and the original contractor, perform any labor or furnish materials in building, altering, repairing, beautifying or ornamenting any house, * * * shall have a lien for the value of such labor and materials upon such house,' etc. The Illinois courts held that the statute did

tended and directed the construction of the work.[1] By the interventions in this foreclosure suit, the question of the rights of furnishers of supplies to the railroad company under the statutes of Kentucky giving statutory liens to certain parties to be preferred to the bondholders, came before the United States Circuit Court of Appeals for the sixth circuit. This rule was declared by the court: Contractors supplying laborers and teams for the construction and repair of a railroad, being paid for the same by the day, and either party having the right to stop work at the end of any day, are not "laborers" or "employees" with the terms of the statute of 1876, which, among other things, gives a lien for work done and materials furnished in keeping the road a going concern, but must rely on the Contractors' Act of 1888, which gives a lien in favor of persons "furnishing labor or materials for the construction or improvement" of any railroad, canal or other public improvement.[2] In the same case this rule was also declared:

not extend and give a lien to a contractor with a sub-contractor. Smith Bridge Co. *v.* Louisville, N. A. & St. L. R. Co., 72 Ill. 506."

[1] Central Trust Co. *v.* Richmond, N. I. & B. R. Co., (1892) 54 Fed. Rep. 723.

[2] Tod *v.* Kentucky Union Ry. Co. (Rosser et al., Interveners), (1892) 52 Fed. Rep. 241, holding that the petition of the intervener was properly dismissed. JACKSON, Circuit Judge, speaking for the court, said: "In Vane *v.* Newcombe, 132 U. S. 220; s. c., 10 Sup. Ct. Rep. 60, the plaintiff, having contracted with the company to erect certain telegraph wires on the company's poles, and furnished the labor of himself and others in doing the work, claimed a priority lien, under a statute of Indiana, which gave a lien to employees of corporations. The Supreme Court said: 'It seems clear to us that Vane was a contractor with the company and not an employee, within the meaning of the statute. We think the distinction pointed out by the Circuit Court is a sound one, namely, that to be an employee, within the meaning of the statute, Vane must have been a servant, bound in some degree, at least, to the duties of a servant, and not, as he was, a mere contractor, bound only to produce or cause to be produced a certain result —a result of labor, to be sure—but free to dispose of his own time and personal efforts according to his pleasure, without responsibility to the other party.' The lien was accordingly denied, and, in Railroad *v.* Wilson, 138 U. S. 501; s. c., 11 Sup. Ct. Rep. 405, it was said that an employee implies continuity of service and excludes those employed for a special or single transaction. In construing the New Jersey statute, which gave laborers of corporations in case of an insolvency a lien upon corporate assets for the amount of wages due them, the Supreme Court of that state held that the right conferred was strictly personal, inhering alone in the person who actually performs the labor or service, and that he who furnishes the labor or services of others under a contract to do the whole business of a corporation, or a particular branch of it, was neither within the letter nor spirit of the act. It was further held

Where supplies, suitable either for the construction of the unfinished part of a railroad or the carrying on of the finished part, are furnished without any contract as to how they shall be used, the materialman has a lien under the act of 1876 for the part actually used in operating the railroad and another lien under the Contractors' Act of 1888 for the part actually used for construction and repairs; but where he had lost the lien under the latter act because of a failure to file his statement within sixty days, the burden of proof was on him to show what part of the supplies was actually used for the operation of the road.[1]

§ 563. **The rule under Ohio statutes.**— The United States Circuit Court of Appeals for the sixth circuit, in the opinion rendered by SWAN, D. J., has held that the right to a lien, under the Ohio statute, relating to liens against railroads, is restricted to claims for labor performed or materials furnished for the construction of the road, depot buildings and water tanks, and cannot be extended to a claim for furnishing an electric lighting plant to hotel premises, at the instance of a railroad company; also, that the General Lien Law of Ohio gave no right to a lien upon a railroad for materials used in and for its construction; nor were materials furnished for the construction of the electric lighting apparatus, railway and power house, within the provision of the General Lien Law of Ohio, giving a right to a lien for machinery and materials furnished for "erecting, repairing or removing a house * * * or other structure.[2]"

§ 564. **Contractors — Tennessee statutes construed.**— In a case involving the right to priority of liens of persons claiming as contractors in the construction of a railroad under the Tennessee statute over those of the mortgage bondholders, the United States Circuit Court of Appeals for the sixth circuit declared these rules: Under the Tennessee statute, relating to railroad contractors' liens, the contractor must deal directly with the company in

by said court that the wages, to be within the protection of the statute, must be due to a person in the employ of the corporation at the time when it became insolvent; that only those in the employ of the corporation at the time of its insolvency were within either the words or policy of the statute. Delaware, L. & W. R. Co. *v.* Oxford Iron Co., 33 N. J. Eq. 196."

[1] Tod *v.* Kentucky Union Ry. Co. (Rosser et al., Interveners), (1892) 52 Fed. Rep. 241.

[2] Industrial & Mining Guaranty Co. *v.* Electrical Supply Co., (1893) 58 Fed. Rep. 732.

order to secure a lien for his work and material. If a sub-contractor, he can have no lien unless he serves notice on the railroad company of the principal contractor's failure to pay him, and unless, at the time of such notice, the company shall owe money to the principal on the contract which the sub-contractor has helped to perform, and the lien is limited to the amount so due the principal contractor. The principal contractor for the construction of this road was a dominant stockholder in the railroad corporation, and the sub-contractors endeavored to fix their liens on the ground that the principal contractor was acting in this transaction as agent of the corporation. Upon the points raised by this suggestion the Court of Appeals declared that the fact that he who made this construction contract with the railroad company was its principal stockholder, and dominated and controlled its action, did not render him an agent of the railroad company, so as to make his individual sub-contracts in law the contracts of the company, where neither he nor the company held out to the sub-contractors the existence of any such agency, or, as between themselves, had any intention of establishing such agency. Further, while construction contracts, made by a dominating stockholder with a railroad company for his own benefit are looked upon with suspicion and have the condemnation of the courts when drawn in question by other stockholders, bondholders, or by the corporation itself, their legal existence cannot be questioned by third persons who are not injured by them, as in this case, by sub-contractors who dealt with the contractor in his individual character.[1] The dominant stockholder in this railroad corporation, who had made a construction contract with the company in his individual character, had failed to pay the sub-contractors who had done the work of construction. These sub-contractors, afterwards, in order to give them and materialmen a lien on the railroad under the Tennessee statute in relation to such liens, through their representatives, acting with the principal contractor, and by means of his control over the board of directors of the railroad company, obtained an acknowledgment on the minutes of the railroad company of an amount still due him, vastly in excess of what was really due him, and more than sufficient to cover all the claims of these sub-contractors. The principal contractor sued for the amount mentioned on the minutes

[1] Central Trust Co. of New York *v.* Bridges, (1893) 57 Fed. Rep. 753.

of the railroad company, and the company's attorney consented to a judgment for that amount. As to the priority rights of this judgment, the United States Circuit Court of Appeals for the sixth circuit held that the judgment was fraudulent as against persons injured thereby, and, as an evidence of its rightfulness as a claim, was of no force when the claim was contested by holders of prior mortgage bonds of the company in a foreclosure suit in a federal court.[1]

§ 565. **Furnishers of supplies — Virginia statutes on this subject construed.**— A holder of the bonds of a railroad company, a Virginia corporation, had recovered judgment on his bonds against the railroad company, and upon his execution being returned "*nulla bona*," instituted an action in equity in the United States Circuit Court for the eastern district of Virginia, setting forth the insolvency of the company, etc., and for the appointment of a receiver, to which the trust company, trustee named in the mortgage securing the bonds, was admitted as a party, and a sale in foreclosure was asked. There were interventions in this suit by a car trust company and others who had furnished supplies to the railroad company, and out of these interventions arose questions of priority of liens of the mortgage bondholders and the furnishers of cars and supplies. The Code of Virginia, section 2462, provides that a conditional sale of rolling stock to a railroad company where legal title is reserved to the vendor until the purchase money is paid shall be void as to creditors and *bona fide* purchasers of the vendee unless the contract is recorded as therein required, and "each locomotive and car * * * be plainly and permanently marked with the name of the vendor on both sides thereof, followed by the new owner." It was held that a lien for the purchase money of rolling stock reserved by contract under this section was in no wise inconsistent with the existence of a lien under the Code of Virginia, section 2485, which gives to all who furnish supplies necessary to the operation of a railway "a prior lien on the franchise, gross earnings and all the real and personal property" of the road upon condition that the claim be recorded as required by the section following it. The cars here were furnished to the railroad company under a contract styled a "lease," which pro-

[1] Ibid.

vided for payment of the purchase money in monthly installments with the right in the vendor on default to take possession of the cars and sell, returning any surplus after payment of the outstanding notes to the vendee. The name of the vendor was put upon the cars as "owner," and the contract was recorded as required in the case of conditional sales. The court held that the cars were "furnished" within the meaning of the Virginia statute declaring a supply lien in such cases, and nothing done by the vendor amounted to a waiver of such lien. As to the bondholders secured by the mortgage on all the property of the road before the cars were furnished, the sellers of the cars were held to be entitled to a prior lien on the property of the railroad company whether their contracts of claims of liens were properly recorded or not, as the mortgage only attached to the cars as after-acquired property, and was, therefore, subject to all existing equities whether there was notice to the mortgagors or not. There was a provision in the statute of Virginia as to the liens of those furnishing supplies to railroad companies that "unless [the furnisher] shall within six months after his claim has fallen due" file in a specified office a prescribed memorandum of his claim to be recorded. The time of furnishing the supplies was held to be immaterial so far as concerned the claim, and where the supplies were to be paid for in installments the claim must be filed and recorded within six months after the last installment falls due. Before some of these cars were furnished an act had been passed in Virginia giving a supply lien, which was held unconstitutional, as its title did not cover the object of the act. Afterwards the laws of the state were codified, including that act, and the act adopting the Code was passed before these cars were furnished, but it did not go into effect until a time later. As to these particular cars there was held to be no lien prior to the bondholders' lien, there being no valid act in existence creating such a lien when they were furnished. It was also held that a creditor's bill being filed against the railroad company, and the court referring the case to a commissioner to determine the claims and their priorities, the effect was to suspend the running of the six months within which the claim of lien was required to be filed by the Code of Virginia, section 2486.[1] Medical services rendered and

[1] Newgass *v.* Atlantic & D. Ry. Co. (Central Car Trust Co. et al., Interveners), (1893) 56 Fed. Rep. 676. On this last point the court followed Seventh

board furnished by a hospital to an employee of the railroad company injured and disabled in its service were held not to be "supplies necessary for the operation of a railroad" within the statute giving a lien for supplies.[1]

§ 566. Loans of money to corporations before receivership.— The mere fact that money loaned to a railroad company was expended in payment of interest on its first mortgage bonds, or operating expenses, does not entitle the lender to preference over the first mortgage bonds by way of subrogation, or on the ground of superior equities. Although advances may have enabled a railroad company to maintain itself as a going concern, that fact alone does not give such advances priority over first mortgage bonds upon the theory that the interest of the public and of the bondholders were subserved by such advances.[2] In this Virginia

National Bank *v.* Shenandoah Iron Co., 35 Fed. Rep. 436.

[1] Newgass *v.* Atlantic & D. Ry. Co. (Central Car Trust Co. et al., Interveners), (1893) 56 Fed. Rep. 676.

[2] Morgan's La. & Tex. R. R. & Steamship Co. *v.* Texas Central Ry. Co., (1890) 137 U. S. 171. "From the account stated," said Chief Justice FULLER, speaking for the court, "it appears that the gross earnings were each year sufficient to pay the operating expenses and taxes, and that the deficit of each year was produced by the payment of interest on the bonded debt. But if the advances could, therefore, be treated as having been specifically procured for or specifically applied to the payment of interest as such (although there is no evidence to that effect), still such payments must afford no basis for the assertion of a preference as against the bondholders. So far as disclosed, the interest coupons were paid, not purchased (Ketchum *v.* Duncan, 96 U. S. 659; Wood *v.* Guarantee Trust Co., 128 U. S. 416), and cannot be set up as outstanding, and the contention is wholly inadmissible that the bondholders, because they received what was due them, should be held to have assented to the running of the road at the risk of returning the money thus paid, if the company, by reason of unrealized expectations on the part of those who made the advances, should ultimately turn out to be insolvent and unable to go on. By the payment of interest the interposition of the bondholders was averted. They could not take possession of the property, and should not be charged with the responsibility of its operation. It is true that a railroad company is a corporation operating a public highway, but it does not follow that the discharge of its public [duties?] excuses it from amenability for its private obligations: If it cannot keep up and maintain its road in a suitable condition and perform its public service for which it was endowed with its faculties and franchises, it must give way to those who can. Its bonds cannot be confiscated because it lacks self-sustaining ability. To allow another corporation, which, for its own purposes, has kept a railroad in operation in the hands of the original company, by enabling it to prevent those who would otherwise be entitled to take it from doing so, a

case bankers held coupons of early mortgage bonds, and had furnished the railroad company money which was used to pay wages and other preferred debts and received its promissory notes. Bonds were afterwards issued, secured on the income of the railroad company, and guaranteed by another company, to fund this indebtedness which was outstanding. These bankers took at sixty per cent the amount of their debt in these income bonds, received prior mortgage bonds as collateral, and surrendered the coupons, which were canceled, but there was no express agreement that their original claims were extingushed. The bankers claimed that they were entitled to a preference over the mortgage bondholders out of the funds to be distributed, upon the ground that as to the coupons there was a mere exchange of securities without affecting the debt of which the coupons were the evidence, and that, as to the promissory notes, the money for which they were given was used in the payment of preferred debts, and, therefore, they were entitled to be subrogated to the rights and privileges of the creditors whose debts were thus paid. Upon the well-settled principle that no mere change in the form of the evidence of a secured debt will discharge the debt, unless so intended, but that where a security is accepted in satisfaction of another the debt is discharged, and this would in general be determined by the surrender or retention of the original security, the Supreme Court of Appeals of Virginia held that these bankers were not subrogated to the lien of their original debt, which was extinguished by the receipt of the promissory notes.[1]

preference in reimbursement over the latter on the ground of superiority of equity would be to permit the speculative action of third parties to defeat contract obligations and to concede a power over the property of others which even governmental sovereignty cannot exercise without limitation. And, if all these advances should be considered as applied in payment of the operating expenses only, on the theory, where such was not literally the fact, that they supplied a deficit created by the payment of interest out of the gross earnings, the same remarks would be applicable." Where loans of money to carry on the business of a railroad corporation will be held to have a priority over the claims of the mortgage bondholders, see Farmers' Loan & Trust Co. *v.* Vicksburg & Meridian R. Co., 33 Fed. Rep. 778.

[1] Fidelity Insurance Trust & Safe Deposit Co. *v.* Shenandoah Valley R. R. Co., (1889) 86 Va. 1. As to the coupons being extinguished, after referring to the statement made by the officers of the company when they made it for the purpose of "listing" the bonded indebtedness of the company not showing any claim to the contrary, one of these claimants then being the president of the company and the other a director, the court

§ 567. Claims for services rendered the corporation prior to the appointment of a receiver.— There was in this case an order appointing the receiver which authorized him to pay out of income, besides current expenses and charges, all wages due to

said: "Upon the strength of these representations, sales of the bonds were no doubt effected to innocent purchasers, and it would now be the grossest injustice to such persons to allow the claims in question as a preferred charge on the mortgaged property, and thereby, to that extent, to impair the security of the mortgages. Plainly upon no just principle can this be done. A decisive authority upon this point is Addison *v.* Lewis, 75 Va. 701. There the president of the railroad company intervened and asserted a claim for several years' salary which accrued before the road went into the hands of a receiver, but as it appeared that in his published annual reports as president for the years in question, his salary for those years was put among the *paid items*, it was held that any right which he might have had to be paid in preference to the bondholders had been waived, although the salary in point of fact had not been paid. This ruling, it seems to us, is eminently just and proper, and in accordance with public policy, inasmuch as the officers of a railroad company are, in a general sense, trustees, and must, therefore, act in the strictest good faith in putting forth statements to the public as to the condition of the affairs of the company upon which innocent third persons, in their dealings with the company, have a right to rely. The same considerations apply to the promissory notes in question. * * * It appears moreover, that when the notes for the loans were taken, the [claimants] received general mortgage bonds of the company as collateral security for their payment, which goes far to show, if it does not conclusively show, that the idea of a right to subrogation is altogether an afterthought. For why take general or second mortgage bonds as collateral if the understanding was that [claimants] were to stand in the place of those whose equities were superior even to the first mortgage? To this question the answer must be, that the money was loaned on the credit of the company and the collaterals so furnished, alone. At all events, such is the fair inference from the record, and there is no evidence to repel it. In Addison *v.* Lewis, 75 Va. 701, a similar claim was asserted on the part of a bank for money advanced by it before the appointment of a receiver, and which was used by the railroad company in paying current expenses. The claim, however, was rejected. The court said: 'The bank discounted the paper of the company solely upon the credit of the company and upon collaterals deposited by the company with the bank. The acceptance of these collaterals was in itself a recognition of the subordination of the claim of the bank to the lien of the bondholders, and is sufficient to estop the bank from setting up the claim preferred in the petition.' The case of Coe *v.* N. J. Midland Rwy. Co., 31 N. J. Eq. 105, and Atkins *v.* Petersburg R. R. Co., 3 Hughes, 307, relied on by the [claimants], are not in point, as in each of those cases the advances were made, at the instance of the debtor, on a distinct understanding, clearly established, that the parties by whom they were made, should be subrogated to the rights of the creditors whose

employees of the railroad company at the date of the order for services within ninety days theretofore. It was held by the United States Circuit Court for the district of South Carolina that a lawyer employed by the company at a fixed salary per month came within the terms of this order and gave him a priority to the bondholders to that extent. But upon his claim for salary for months prior to the ninety days and for money advanced by him in connection with rendering his services, they held that he was not entitled, on the appointment of the receiver in foreclosure proceedings, to receive payment out of the proceeds of the sale, prior to the satisfaction of the mortgage bonds, even though the earnings of the road had been improperly diverted from current expenses for the benefit of bondholders, or the equity to a return of diverted earnings applied only in favor of those who have helped to keep the road a going concern. He was allowed to take a judgment against the railroad company for so much of his claim as was not performed, and his right to retain papers in his hands for the whole claim was recognized.[1] The court also held that legal services rendered to the railroad company in maintaining before the courts the validity of municipal aid bonds, were not of a character to take precedence of the company's mortgage bonds, within the doctrine of Fosdick *v.* Schall, 99 U. S. 235, and equity had no authority to give them such precedence, especially where the services were rendered two years before the appointment of the receiver. Nor would the fact that such services resulted in benefit to the bondholders, justify displacing the lien of the bondholders when they were not parties to the contract of employment.[2] In this foreclosure suit, upon the intervention of one who had been the general passenger and freight agent of a navigation company which had a business connection with the railroad company involved here, the United States Circuit Court for the district of South Carolina held that the company having passed into the hands of a receiver, the intervener had a valid claim for the arrears of his salary as gen-

debts were paid with the money advanced." See 3 Pom. Eq. § 1212, and cases in the notes.

[1] Finance Co. of Pennsylvania *v.* Charleston, C. & C. Ry. Co. (Moon, Intervener), (1892) 52 Fed. Rep. 526. See as to first ruling, Railroad Co. *v.* Wilson, 138 U. S. 505; s. c., 11 Sup. Ct. Rep. 405.

[2] Finance Co. of Pennsylvania *v.* Charleston, C. & C. R. Co. (Shand et al., Interveners), (1892) 52 Fed. Rep.

eral freight and passenger agent, but had no equity, as he claimed, to be paid in priority to the mortgage creditors.[1]

§ 568. **When cases are not properly removable to United States court from state court.**— Where a case involving railroad bonds had been removed to the United States Circuit Court by order of a state court upon the ground of "prejudice or local influence," JACKSON, Circuit J., remanded the case to the state court. His holdings upon the questions involved were that when, in a suit by persons owning certain "equipment bonds" of a railroad company, the United States Supreme Court decides that such bonds constitute no lien on the property, and subsequently a State Supreme Court, in a suit on other bonds of the same issue, reaches an opposite conclusion, this latter decision cannot be considered as showing "prejudice or local influence," so as to constitute a ground for removing a third suit in a subordinate court of the state, on still other bonds of the series, to the Federal Circuit Court. As to the interest of removing defendants, it was held that in a suit to assert the lien of such railroad equipment bonds, the trustees under mortgages to secure subsequent issues of bonds had no interest in the controversy as parties defendant, such as would give them a right to remove the cause to a federal court, where their mortgages had all been foreclosed and the property sold to a new corporation. Under a valid decree of a court of competent jurisdiction as to citizenship of parties, it was held that where in a suit by a corporation in a state court against several railroad companies, their trustees and mortgagees, on certain equipment bonds, the lien whereof was denied by answer, many other holders of the same series of bonds were permitted, with plaintiff's consent, to become parties defendant, and by cross-bills to set up the lien of their bonds; that in determin-

678. See Hand *v.* Railroad Co., 21 S. C. 162; Bound *v.* Railway Co., 51 Fed. Rep. 60.

[1] Bound *v.* South Carolina Ry. Co. (Quintard, Intervener), (1892) 50 Fed Rep 312. The district judge, SIMONTON, called attention to the fact that the doctrine of Fosdick *v.* Schall, 99 U. S. 235, had never been applied in any case except that of a railroad, and cited Wood *v.* Guarantee Trust & Safe Deposit Co., 128 U. S. 421; s. c., 9 Sup. Ct. Rep. 131, involving water works bonds and coupons, in which the point was pointed out by the justice delivering the opinion, but the court did not find it necessary to decide it. SIMONTON, D. J., held that it did not apply, and very fully discusses the matter of the distinction

ing whether the citizenship of the parties was such as to warrant a removal to the Federal Circuit Court on the ground of prejudice and local influence, all the parties asserting the lien of the bonds should be considered as parties plaintiff; and that when part of the plaintiffs, as thus arranged, were aliens, and others were residents of the same state with some of the remaining defendants, the federal court had no jurisdiction.[1]

between railroad corporations and other private corporations in this regard.

[1] Adelbert College of Western Reserve University *v.* Toledo, W. & W Ry. Co., (1891) 47 Fed. Rep. 836.

CHAPTER XXXI.

TAXATION BY PUBLIC CORPORATIONS.

§ 569. General rules.
570. Exemption from taxes.
571. License tax.
572. Assessment of taxes for benefits.
573. When a levy of taxes by a school district is not authorized.
§ 574. Irregularity in the levy of taxes.
575. When an assessment cannot be attacked.
576. Federal taxation of incomes.
577. Injunction of a collection of taxes.

§ 569. **General rules.**— It is within the power of the legislature to authorize a city to impose a yearly tax upon corporations doing business within the limits of the city.[1] A city will be precluded from levying a license tax on an express company by the provision in a statute that express companies shall pay a privilege tax to the state, and that no company which has paid such tax shall be liable to pay any other tax in the state.[2] In determining whether the percentage of a tax levy is in excess of the limit prescribed by statute to the city, a yearly deposit in the taxes collected as regards the amount levied cannot be taken in account.[3] The making of a subsequent levy of taxes, which, together with the original levy, may exceed the limit of taxation imposed by law upon a city, will not render invalid the levy originally made, which was not in excess of the limit.[4] Though a municipal election had resulted in a majority of votes against the issue of bonds for school purposes mentioned in the statute, which provided for the raising of revenue for school purposes by a city of the state of Georgia, the Supreme Court of the state held that under the statutes the mayor and council might levy an annual tax for school purposes.[5] A public corporation authorized to tax professions, trades, incomes and franchises, has been held not to be bound to tax them uniformly as to amount.[6] The right to levy taxes is conferred upon a town by a provision in its charter to

[1] Harrisburg City *v.* Pennsylvania Telephone Co., 15 Pa. Co. Ct. Rep. 518.

[2] Douglass *v.* City of Anniston, (Ala.) 16 So. Rep. 133.

[3] Bassett *v.* City of El Paso, (Tex. Civ. App.) 28 S. W. Rep. 554.

[4] Bassett *v.* City of El Paso, (Tex.) 30 S. W. Rep. 893.

[5] Ayers *v.* McCalla, (Ga.) 22 S. E. Rep. 295.

[6] State *v.* Worth, (N. C.) 21 S. E. Rep. 204.

"pass such rules and ordinances as may be necessary * * * for the levying of taxes."[1] The statute of Missouri in regard to the levy of school taxes on railroads provides for the furnishing by the school board of an estimate of the amount of funds necessary to sustain the schools to the county clerk, "stating clearly the amount deemed necessary for each fund and the rate required to raise the amount." The Supreme Court of Missouri has held that the value of the property to be assessed having been ascertained, the failure in the report of the school board to specify the amount of each fund did not invalidate the tax, if the rate necessary to raise the same was stated, as the amounts might be calculated from the data given.[2] School directors are empowered by a statute of Illinois to levy taxes not exceeding two per cent for educational purposes and three per cent for building purposes. A tax for educational purposes of more than two per cent has been held by the Supreme Court of the state to be void as to the excess, even though the taxes levied for the two purposes did not exceed five per cent.[3] That a school district has illegally levied and collected taxes on lands in another school district will not prevent the latter from levying and collecting taxes on the same lands.[4] The trustees of a school district having repaired a lawfully condemned school house out of their own private funds, property owners cannot avoid a tax afterwards lawfully imposed to pay for the repairs.[5] A special assessment on the property of a school district to raise the money will be authorized by a vote of the electors of the district to appropriate moneys for school purposes, and to issue bonds for raising it.[6] Failure to prefix to their tax list a heading "showing for what purpose the different items of a tax is levied," required by the statute of New York, by the trustees of a school district, has been held not to vitiate the assessment of taxes made by them, the provision being directory only.[7] The object of a meeting of the voters

[1] State *v.* Hoff, (Tex. Civ. App.) 29 S. W. Rep. 672.

[2] St. Louis & Santa Fe Ry. Co. *v.* Gracy, (Mo.) 28 S. W. Rep. 736.

[3] Chicago & A. R. R. Co. *v.* People, 155 Ill. 276; s. c., 40 N. E. Rep. 602.

[4] Arthur *v.* School District of Polk Borough, 164 Pa. St. 410; s. c., 30 Atl. Rep. 299; 35 W. N. C. 289.

[5] Louisville & Nashville R. R. Co. *v.* Trustees School District No. 108 (Ky.) 29 S. W. Rep. 340.

[6] Chamberlain *v.* Board of Education of Cranbury Township in Middlesex County, (N. J.) 31 Atl. Rep. 1033 See, also, State *v.* City of Omaha, 39 Neb. 745.

[7] Thomson *v.* Harris, 34 N. Y. Supp. 885.

of a school district in Oregon was stated in the notice for the meeting to be "to levy a tax of 8½ mills for building a school house, and a tax of 1½ mills for the teachers' fund." A motion at the meeting that "we proceed to vote on the 10-mill tax" was held by the Supreme Court of Oregon sufficient to indicate that the tax referred to was that mentioned in the notice.[1] The statutes of Illinois require school directors to certify the amount of money required to be levied by special tax. A certificate of school directors that "we require the amount of two dollars on each one hundred dollars to be levied as a special tax for that purpose, and one dollar on each one hundred dollars for building purposes on the taxable property of our district for the year 1894" has been held, though irregular in form, not to be void.[2] A school district having power to levy an *ad valorem* tax or a poll tax, or both, should the trustees levy a tax on the property in the district for the repair of a condemned school house, the tax will not be rendered invalid by failure to levy a poll tax.[3]

§ 570. **Exemption from taxes.**—Where a municipality is authorized to tax *all* property it can exempt none, as delegated power to tax does not imply power to exempt from taxation.[4] It

[1] Vaughn *v.* School District No. 31 of Tillamook County, (Or.) 39 Pac. Rep. 393.

[2] Chicago & A. R. R. Co. *v.* People, 155 Ill. 276; s. c., 40 N. E. Rep. 602.

[3] Hunter *v.* Louisville & Nashville R. R. Co., (Ky.) 30 S. W. Rep. 645.

[4] Whiting *v.* Town of West Point, (1892) 88 Va. 905, awarding a writ of mandamus to compel the municipal authorities to assess the property of a corporation which, by ordinance, had been exempted from taxation. The court cited, in support of the text, Cooley on Taxation, 200; State *v.* Hannibal & St. J. R. Co., 75 Mo. 209; Austin *v.* Gas Company, 69 Tex. 180; Wilson *v.* Supervisors, 47 Cal. 91. It was then said: "These authorities, which are only a few of the many that might be cited to the same effect, show that the rule requiring all municipal powers to be construed strictly, applies especially to a case like the present. And the reason, as already suggested, is this: That the power of taxation, being an attribute of sovereignty, can be exercised only by the sovereign. Hence, when delegated by the legislature to a municipal corporation, the latter is considered, as *pro hac vice* the agent of the state, acting for the benefit of the municipality. In other words, the municipality, in the eye of the law, is the hand of the state by which the tax is laid and collected. Therefore, the statutory authority must be strictly pursued; for as an agency to sell does not imply an agency to buy, so neither does a delegated power to tax imply a power to exempt." That in taxation the municipality acts for the state, see Gilman *v.* City of Sheboygan, 2 Black, 510; Langhorne *v.* Robinson, 20 Gratt. 661; City of Richmond *v.* Richmond & D. R. R. Co., 21 Gratt. 604.

was attempted in this case to restrain a city of Pennsylvania from taxing the property of a corporation which published, bought and sold books for a profit, on the ground that it was a purely public charity. The Court of Common Pleas held that it could not have total exemption from taxation, on the ground that it sold at less than cost, or evenly gratuitously distributed some books.[1] The Supreme Court affirmed this decision, holding that a society organized as an institution of purely public charity, and as such exempted from taxation, may, as an aid to the accomplishment of its primary object, carry on business, or use part of its property for a business purpose, which will render such business or such part of its property taxable.[2] As to the exemption of church property from municipal corporation tax under the statutes of Pennsylvania, the Supreme Court of that state has held that under no circumstances is a church entitled to exemption from taxes on its property for more than the portion of the tax year during which it actually holds the title to the property; also, that under the statute of May 14, 1874 (P. L. 158), where church property is rented out and produces income or revenue, it is subject to taxation, although for a part of the time, certain days or hours of the week, the church also uses the rented portion for its own purposes.[3] They also declared the further rule that where a part of a building may be used solely for church purposes, and certain rooms in the building be rented for a school, the building may be divided for purposes of taxation, and the portion *used solely* for church purposes be declared exempt from taxation.[4] Under the Pennsylvania statutes a library building is subject to municipal taxation upon so much thereof as is rented and produces a revenue, although it might be otherwise exempt. Charging a price for the use of its books when they are taken out and

[1] American Sunday School Union *v.* Philadelphia, (1894) 14 Pa. Co. Ct. Rep. 213.

[2] American Sunday School Union *v.* City of Philadelphia, (1894) 161 Pa. St. 307. In Philadelphia *v.* Masonic Home of Penn., (1894) 160 Pa. St. 572, it was held that a home limited to indigent, afflicted and aged Free Masons, although supported by voluntary contributions, without charge to the beneficiaries and with no profit either to the corporation or its officers, was not a "purely public charity," exempt from taxation within the meaning of the Constitution and statutes of Pennsylvania.

[3] Philadelphia *v.* Barber, (1894) 160 Pa. St. 123; Sewickley Borough *v.* Sholes, 118 Pa. St. 165, distinguished.

[4] Philadelphia *v.* Barber, (1894) 160 Pa. St. 123.

annual dues from its members will not deprive the association of its exemption.[1] Where, by the opening of a city street, a part of the land used for a charitable institution, and not taxed, was cut off from the main lot, and it was put to no other use, it has been held that it was still exempt from taxation by the city.[2] The case stated in a Pennsylvania case, and agreed upon in an action by a county to secure taxes against a street railway company, declared "that the said lot and stables and the said horses, cars and vehicles are used only in and about the business of carrying passengers and produce, according to the defendant's corporate powers, and that they are appurtenant, necessary and indispensable therefor." The Supreme Court held the agreement above stated brought the case within the principle that the property of canal and railroad companies, and other *quasi* public corporations, necessary for the exercise of their several franchises as depots, houses and water stations, is not taxable for local purposes. The reason for this exemption is that these things enter into the very composition of the works of these corporations, and are essential to the exercise of their corporate functions, and for this reason are taxed by the state as included in the capital of corporations.[3] This court in another case declared that railroads, canals and gas companies must have the right of eminent domain in order to perform their functions. Their property, which is indispensable to their chartered rights, is represented by their capital stock, and

[1] Mercantile Library Company *v.* Philadelphia, (1894) 14 Pa. Co. Ct. Rep. 204; affirmed in Mercantile Library Co. *v.* City of Philadelphia and Taylor, Receiver of Taxes, (1894) 161 Pa. St. 155, upon the authority of Philadelphia *v.* Barber, (1894) 160 Pa. St. 123. See Donohugh *v.* Philadelphia Library Co., 86 Pa. St. 306; Young Men's Christian Association *v.* Donohugh, 7 W. N. C. 208.

[2] Ladies' United Aid Society, etc. (Methodist Home), *v.* Philadelphia, (1894) 14 Pa. Co. Ct. Rep. 215. The cases upholding assessments upon such property for improvements were distinguished. Wilkinsburg Borough *v.* Home for Aged Women, 131 Pa. St. 109; Philadelphia *v.* Pennsylvania Hospital, 134 Pa. St. 171, and 143 Pa. St. 368. The court said: "This is upon the ground that a claim of that kind, although called a tax, is in reality an assessment for benefits done to the property. It proceeds upon the theory that the property is made more valuable by the improvement of the street in front of it. It is charged once for all time."

[3] Northampton County *v.* Easton Passenger Railway Co., (1892) 148 Pa. St. 282; citing Westchester Gas Company *v.* County of Chester, 30 Pa. St. 232; County of Erie *v.* Western Transportation Co., 87 Pa. St. 434; Coatesville Gas Co. *v.* County of Chester, 97 Pa. St. 476.

as such is taxed specially by the legislature, and the law will not subject it to duplicate taxation by mere inference.[1]

§ 571. **License tax.**—The United States Supreme Court held that an ordinance requiring agents soliciting orders on behalf of manufacturers of goods to take out a license and pay a tax therefor, made by a municipal corporation under authority conferred by a statute of the state granting to such corporations power to levy and collect license taxes on hawkers, peddlers and merchants of all kinds, was an exercise, not of the police power, but of the taxing power, and when it was enforced against an agent sent by a manufacturer of goods in another state to solicit orders for the products of his manufactory, it imposed a tax upon interstate commerce, in violation of the provisions of the Constitution of the United States.[2] A telegraph company, a New York corporation, which had accepted the provisions of the act of congress,[3] whereby it put its lines at the service of the United States for postal, military and other purposes, and gave precedence to its business, sought to restrain the officers of the city of Charleston, South Carolina, from the collection of a license of $500, imposed upon it by an ordinance of the city, made under power conferred by a state statute in the United States Circuit Court for that district. On appeal to the United States Supreme Court the latter court held that the imposition of the license fee being upon business done exclusively within the city, and not including any business done to or from points without the state and not including any business done for the government of the United States, its

[1] Schuylkill County *v.* Citizens' Gas Co., (1892) 148 Pa. St. 162, holding that the gas pipes of the incorporated company for the supply of natural gas to consumers were not assessable *eo nomine* for local taxation either as land or as a part of the company's capital stock. The court, however, held that a house upon the land of the gas company occupied by a tenant was not a necessary part of the company's works or equipment, and was, therefore, taxable. See, also, Allegheny Co. *v.* McKeesport Diamond Market, 123 Pa. St. 164.

[2] Brennan *v.* Titusville, (1894) 153 U. S. 289. The court cited and commented upon the following cases in support of its ruling: Brown *v.* Maryland, 12 Wheat. 419, 444; Welton *v.* Missouri, 91 U. S. 275, 278; Leloup *v.* Mobile, 127 U. S. 640, 645; Robbins *v.* Shelby Taxing District, 120 U. S. 489; Asher *v.* Texas, 128 U. S. 129; Stoutenburgh *v.* Hennick, 129 U. S. 141; Lyng *v.* Michigan, 135 U. S. 161, 166; McCall *v.* California, 136 U. S. 104, 111; Crutcher *v.* Kentucky, 141 U. S. 47, 61; Ficklen *v.* Shelby County, 145 U. S. 1.

[3] Approved July 24, 1866, chap. 230; 14 Stat. 221; New Rev. Stat. § 5263.

officers or agents, was an exercise of the police power, and was not an interference with interstate commerce.[1]

§ 572. **Assessment of taxes for benefits.**—It is within the discretion of municipal authorities for a local improvement to require the special benefits accruing from such improvement to be assessed upon the property specially benefited, or to impose the same by way of special taxation. When an ordinance is passed authorizing a local improvement, it has the effect of creating a taxing district. Such a taxing district comprises all the property contiguous to the improvement, subject to special taxation for making the improvement. Special assessments and special taxes imposed for local improvements, unlike general taxes, are based upon benefits to the property against and upon which they are assessed and levied, arising from its increased value in consequence of the improvement. They proceed upon the basis of benefits to the particular property, and are authorized only when the local improvement, either actually or presumptively, benefits the particular property in an amount equal to the burden imposed. The levy being upon the basis of benefits accruing to the specific property, it becomes a charge only upon and against it, and liability for the tax is confined to that particular property.[2] The proceedings in the matter of levying assessments for a public improvement, it was contended in an Illinois case, were unwarranted, for the reason, among others, that the supervisor and assessor of the town, who had acted for the town in the matter, were not corporate authorities, within the meaning of the Constitution of the state authorizing the legislature to vest the corporate authorities of cities, towns and villages with power to make local improvements by special assessment. The Supreme Court

[1] Postal Telegraph Cable Co. *v.* Charleston, (1894) 153 U. S. 692. Cases cited by the court as to taxation, and whether in violation or not of the interstate commerce provisions of the Constitution: Telegraph Co. *v.* Texas, 105 U. S. 460; Ratterman *v.* Western Union Telegraph Co., 127 U. S. 411; State Freight Tax, 15 Wall. 232; West. Union Tel. Co. *v.* Alabama, 132 U. S. 472; Pacific Express Co. *v.* Seibert, 142 U. S. 339.

[2] Lightner *v.* City of Peoria, (1894) 150 Ill. 80. See Davis *v.* Litchfield, 145 Ill. 313; Craw *v.* Village of Tolono, 96 Ill. 256; Bloomington *v.* Chicago & Alton R. R. Co., 134 Ill. 452; White *v.* People, 94 Ill. 607; Enos *v.* Springfield, 113 Ill. 65; McLean County *v.* City of Bloomington, 106 Ill. 209; English *v.* City of Danville, 150 Ill. 92; Dunham *v.* Village of Hyde Park, 75 Ill. 371; Fagan *v.* City of Chicago, 84 Ill. 231.

held that the supervisor and assessor were the corporate authorities of a town, and special assessments for local improvements made by them were made by the corporate authorities of the town within the meaning of the Constitution.[1] A statutory direction that an assessment for benefits shall be levied upon each *separate* lot or parcel of land, or upon the *several* lots or parcels of land, has been held in New Jersey not to authorize the assessors to levy distinct assessments upon the component parts of a tract of land which the owner had always treated as an entirety. And it appearing that the commissioners authorized to levy an assessment for the construction of a sewer upon an entire tract of land on which were buildings, had ignored the existence of the buildings and levied distinct assessments upon the parts of the tract, dividing it by lines which intersected the buildings, the court held the assessment illegal, as it could not infer that the benefit accruing to the entire tract was the aggregate of these distinct assessments.[2] The principle of frontage assessment is not necessarily wrong. If that mode properly distributes the benefits among the owners of property benefited, there can be no objection to its use.[3] And where an ordinance provides for an improvement complete in itself, it will not follow that the ordinance is to be deemed void, because the utility of the improvement might be enhanced by the addition of something more which has been omitted.[4] It is no valid objection to a special tax for grading or paving a street, that the city or village is not required to pay the cost of improving the street intersections.[5] This court has also held that municipal authorities in cities and villages organized under the general law of Illinois for the incorporation of such municipalities have no power to provide that the cost of sprinkling its streets shall be paid by special assessment; the sprinkling of streets not being a local improvement, within the meaning of the statute authorizing cities and villages to make

[1] Jones *v.* Town of Lake View, (1894) 151 Ill. 663; citing Hundley *v.* Lincoln Park Commissioners, 67 Ill. 559; People *v.* Gage, 83 Ill. 486; People *v.* Salomon, 51 Ill. 37; People *v.* Mayor, 51 Ill. 18.

[2] The State, Muller, Prosecutor, *v.* Mayor & Council of City of Bayonne, (1892) 55 N. J. L. 102.

[3] The State, Raymond, Prosecutor, *v.* Mayor & Council of Borough of Rutherford, (1892) 55 N. J. L. 441; Jersey City *v.* Howeth, 30 N. J. L. 521; State, Pudney, Prosecutor, *v.* Passaic, 37 N. J. L. 65.

[4] Vane *v.* City of Evanston, (1894) 150 Ill. 616.

[5] Holt *v.* City of East St. Louis, (1894) 150 Ill. 530; upon the authority of Walters *v.* Town of Lake, 129 Ill. 23.

local improvements by special assessment. They further held that the power of a city or village to provide for the sprinkling of streets by special assessment was not expressly given, nor did it arise, by implication, from the powers expressly conferred, nor was it essential to the declared objects and purposes of the corporation. And an attempt by the municipal authorities to declare a purely private work a local improvement, within the meaning of the statute, would be *ultra vires*. While the power of a city council to declare what shall be local improvements is necessarily implied from the power to make the same, this implication can exist only in respect of improvements which cities and villages are authorized to make by special assessment or special taxation.[1] Assessments by commissioners for benefits and street improvements, where they have been on the ground and examined the premises and made their report of estimates according to the principles prescribed in the charter of a municipality, will not be set aside upon conflicting evidence of the justice or sufficiency of such assessments.[2] But when the proceedings of a board of commissioners of assessment are irregular and not in conformity to the municipal charter, the landowner may have them reviewed by *certiorari*, notwithstanding the fact that the charter gives the landowner, who presents to the board of public works written objections to the award made to him, a right to bring suit and have a trial by jury.[3] But a city cannot, by accepting and adopting an improvement of a street, compel property owners to pay for it by special assessment or special taxation.[4]

[1] City of Chicago *v.* Blair, (1894) 149 Ill. 310.

[2] The State, Simmons, Prosecutor, *v.* City of Passaic, (1893) 55 N. J. L. 485; State, Pudney, *v.* Passaic, 37 N. J. L. 65; Hunt *v.* Rahway, 39 N. J. L. 646; Hunt *v.* Rahway, 40 N. J. L. 615; Butler *v.* Passaic, 44 N. J. L. 171; Jelliff *v.* Newark, 48 N. J. L. 101; Hegeman *v.* Passaic, 51 N. J. L. 109.

[3] State, Walls, Prosecutor, *v.* Mayor & Aldermen of Jersey City, (1893) 55 N. J. L. 511; State *v.* Cassidy, 38 N. J. L. 437.

[4] City of East St. Louis *v.* Albrecht, (1894) 150 Ill. 506. The court said: "In City of Carlyle *v.* County of Clinton, 140 Ill. 512, after citing [certain sections of the law authorizing local improvements], we said: 'From these sections of the statute it is apparent that when a city undertakes to make a public improvement, the cost of which they expect to raise by special assessment or special taxation, the first step to be taken is the passage of an ordinance. The ordinance lies at the foundation of the proceeding, and unless the ordinance is passed there is nothing upon which the proceeding can rest. Section 1 confers power to make local improvements by special assessment or special taxation, as the city authorities shall by ordinance pre-

§ 573. **When a levy of taxes by a school district is not authorized.**— In a case where the board of education of a school district, consisting of a president and six members, met and passed an order that $10,000 be raised by special taxation for the current year, which was signed by three persons designated as directors of schools, but who in fact were members of the board of education, the Illinois Supreme Court held that the certificate did not authorize the levy of any tax, and that the proceedings to levy, extend and collect such tax were null and void.[1]

§ 574. **Irregularity in the levy of taxes.**— The same court in a taxpayers' suit for injunction of the treasurer of a county against collection of certain taxes held that mere irregularities in the levying of taxes or the making of assessments would not avoid their collection; and where any part of a tax or an assessment is due, that part must be paid, or at least an offer be made to pay it, before suit would lie to enjoin the collection of what might be alleged to be illegal. In this particular they held that an injunction would not lie on account of the fact that provision was made for collecting a part of the assessment for the construction of a free gravel road before it was actually needed for the payment of bonds or interest to become due.[2]

scribe. This language does not contemplate that the city council shall go on and make the improvement, and, after it is completed, levy and collect a special assessment or tax for such improvement. * * * These sections of the statute are plain, and all point in one direction, that the first step to be taken when a local improvement is to be made, and to be paid for by special assessment or special taxation, is the passage of an ordinance by the city council. Until an ordinance is passed as required by the statute, no work can be done or expense incurred which can become a charge on the property of the landowner.'"

[1] People ex rel. Woody, Collector, *v.* Smith, (1894) 149 Ill. 549. The court said: "We held in Weber *v.* Ohio & Mississippi Railway Co., 108 Ill. 451, that the certificate which the school directors are empowered to make by the school law is the only basis for the imposition of special taxes for school purposes, and said: 'In a sense such certificates are jurisdictional, and any tax extended for school purposes where no such certificate has been returned by the directors, as required by the statute, is without authority of law, and null and void.' See, also, Leachman *v.* Dougherty, 81 Ill. 324; Peoria, Decatur & Evansville Railway Co. *v.* Commissioners, 116 Ill. 232; Ohio & Mississippi Railway Co. *v.* Commissioners, 117 Ill. 280; Lawrence *v.* Traner, 136 Ill. 474."

[2] Florer, Treasurer, *v.* McAffee, (1893) 135 Ind. 540; citing City of Delphi *v.* Bowen, 61 Ind. 29; Foresman *v.* Chase, 68 Ind. 500; Mullikin *v.* Reeves, Treasurer, 71 Ind. 281; Stilz *v.* City of Indianapolis, 81 Ind. 582; Volger *v.* Sidener, 86 Ind. 545; Miles, Treasurer, *v.* Ray, 100 Ind.

§ 575. **When an assessment cannot be attacked.**—The action of a county board of equalization in Indiana has been held not subject to collateral attack by injunction or otherwise, unless the assessment be void, and not merely erroneous, and the Supreme Court reversed the court below, which had granted an injunction to the corporation complaining, restraining the collection of the taxes assessed against it.[1]

166; Bothwell *v.* Millikan, 104 Ind. 162. The court, in Florer, Treasurer, *v.* McAffee, *supra*, said: "The duplicate being put into the hands of the treasurer and being legal on its face, was sufficient to justify the treasurer in collecting the assessments, unless it be shown that some essential requirement of the law was not observed in its preparation or in the proceedings upon which its preparation was based. *Prima facie*, the duplicate is sufficient authority for the collection of the assessments. Noland *v.* Busby, 28 Ind. 154; Rutherford *v.* Davis, 95 Ind. 245; Adams *v.* Davis, 109 Ind. 10." In support of the second ruling it was said: "Those having charge of the collection of funds to meet the obligations of the county are required to use diligence, and they must also be allowed the exercise of good judgment in providing in time for the payment of such obligations so that the credit of the county may not be impaired. Rickets *v.* Spraker, 77 Ind. 371."

[1] Jones, Treasurer, *v.* Rushville Natural Gas Co., (1893) 135 Ind. 595. The court said: "This case is, we think, easily distinguished from the case of Hyland, Auditor, *v.* Brazil Block Coal Co., 128 Ind. 335. In that case it was a conceded fact that the capital stock was all invested in tangible property, which had been returned for taxation, and that the capital stock did not exceed in value the tangible property. The question, however, as to whether the action of the board of equalization could be attacked collaterally was not argued or decided, while that question in this case is squarely made. The board of equalization not only has the power to assess the capital stock of a corporation where the value of such stock exceeds the value of the tangible property, but it is its duty to do so. Rev. St. § 6358; Hyland, Auditor, *v.* Central Iron & Steel Co., 129 Ind. 68. The board, in such cases, has exclusive, original jurisdiction, and, while its action is not strictly judicial, it is at least *quasi* judicial, and binds every one within its jurisdiction. Wilkins *v.* State, 113 Ind. 514; Kuntz *v.* Sumption, Treas., 117 Ind. 1. It is true that such board cannot legally assess capital stock where the capital is invested in tangible property listed for taxation, unless such stock exceeds in value the property in which it is invested; but who shall determine the question as to whether the stock is of greater value than the tangible property? The board of equalization, we think, must decide that question. If it makes a mistake and reaches a wrong conclusion, can it be said that its assessment is void? We think not. We think it is binding on the corporation assessed until set aside or vacated by appeals or some other authorized direct proceeding. * * * We think it is settled, by abundant authority, that the action of the board of equalization, in a matter over which it has jurisdiction, binds every one interested in such matter." See Board *v.* Senn, 117 Ind. 410; Cooley on Taxation, 747, 748; Small, Rec., *v.* City of Lawrenceburgh, 128 Ind. 231.

§ 576. **Federal taxation of incomes.**— The United States Supreme Court, when the question of the constitutionality of the income tax imposed by the government upon the income of corporations and citizens, upon a bill filed by a stockholder of a trust company to prevent its voluntarily making returns for the imposition and payment of such tax, upheld the jurisdiction of a court of equity to grant the relief asked.[1] Upon the merits of the case made by this stockholder's bill to restrain a voluntary return by the corporation required by the Income Tax Act, the majority of the Supreme Court of the United States held that the income tax imposed by congress, so far as it proposed to levy a tax on the rents or income of real estate, was a direct tax within the meaning of the Constitution, and not being apportioned as required by that instrument was repugnant to the Constitution and invalid.[2] Upon the merits of the case made by this stockholder's bill, the United States Supreme Court, HARLAN and WHITE, JJ., dissenting, held that the income tax imposed by congress, so far as it levied a tax on the rents or income of real estate, was in violation of the Constitution of the United States, and invalid.[3] The Income Tax Act provided "that nothing

[1] Pollock *v.* Farmers' Loan & Trust Company, (1895) 157 U. S. 429. FULLER, Ch. J., rendering the opinion for the court, said: "The jurisdiction of a court of equity to prevent any threatened breach of trust in the misapplication or diversion of the funds of a corporation by illegal payments out of its capital or profits has been frequently sustained. Dodge *v.* Woolsey, 18 How. 331; Hawes *v.* Oakland, 104 U. S. 450. As in Dodge *v.* Woolsey, this bill proceeds on the ground that the defendants would be guilty of such breach of trust or duty in voluntarily making returns for the imposition of, and paying, an unconstitutional tax; and, also, on allegations of threatened multiplicity of suits and irreparable injury. The objection of adequate remedy at law was not raised below, nor is now raised by appellees, if it could be entertained at all at this stage of the proceedings; and, so far as it was within the power of the government to do so, the question of jurisdiction, for the purpose of the case, was explicitly waived on the agreement. The relief sought was in respect of voluntary action by the defendant company, and not in respect of the assessment and collection themselves. Under these circumstances, we should not be justified in declining to proceed to judgment upon the merits. Pelton *v.* National Bank, 101 U. S. 143, 148; Cummings *v.* National Bank, 101 U. S. 153, 157; Reynes *v.* Dumont, 130 U. S. 354."

[2] Pollock *v.* Farmers' Loan & Trust Co., (1895) 157 U. S. 429.

[3] Pollock *v.* Farmers' Loan & Trust Co., (1895) 157 U. S. 429. The case mainly relied upon to uphold the constitutionality of the Income Tax Act was Hylton *v.* United States, 3 Dall. 171. FULLER, Ch. J., reviewed

herein contained shall apply to states, counties or municipalities." It was contended before the United States Supreme Court on the part of the government that although the property or revenues of the states or their instrumentalities could not be taxed, nevertheless the income derived from state, county and municipal

the various other cases to which the court's attention was called in these words: "In Pacific Insurance Co. *v.* Soule, 7 Wall. 433, the validity of a tax which was described as 'upon the business of an insurance company' was sustained on the ground that it was 'a duty or excise,' and came within the decision in Hylton's case. The arguments for the insurance company were elaborate and took a wide range, but the decision rested on narrow ground, and turned on the distinction between an excise duty and a tax strictly so termed, regarding the former a charge for a privilege, or on the transaction of business, without any necessary reference to the amount of property belonging to those on whom the charge might fall, although it might be increased or diminished by the extent to which the privilege was exercised or the business done. This was in accordance with Society for Savings *v.* Coite, 6 Wall. 594; Provident Institution *v.* Massachusetts, 6 Wall. 611, and Hamilton Company *v.* Massachusetts, 6 Wall. 632, in which cases there was a difference of opinion on the question whether the tax under consideration was a tax on the property and not upon the franchise or privilege. And see Van Allen *v.* The Assessors, 3 Wall. 573; Home Insurance Co. *v.* New York, 134 U. S. 594; Pullman Company *v.* Pennsylvania, 141 U. S. 18. In Veazie Bank *v.* Fenno, 8 Wall. 533, 544, 546, a tax was laid on the circulation of state banks, or national banks paying out the notes of individuals or state banks, and it was held that it might well be classed under the head of duties and as falling within the same category as Soule's Case, 7 Wall. 433. It was declared to be of the same nature as excise taxation on freight receipts, bills of lading and passenger tickets issued by a railroad company. And referring to the discussion in the convention which framed the Constitution, Mr. Chief Justice CHASE observed that what was said there 'doubtless shows uncertainty as to the true meaning of the term direct tax; but it indicates also an understanding that direct taxes were such as may be levied by capitation, and on lands and appurtenances; or perhaps by valuation and assignment of personal property upon general lists. For these were the subjects from which the states at that time usually raised their principal supplies.' And in respect of the opinions in Hylton's case, the chief justice said: 'It may further be taken as established upon the testimony of Paterson, that the words direct taxes, as used in the Constitution, comprehended only capitation taxes and taxes on land, and perhaps taxes on personal property by general valuation and assessment of the various descriptions possessed within the several states.' In National Bank *v.* United States, 101 U. S. 1, involving the constitutionality of section 3413 of the Revised Statutes, enacting that 'every national banking association, state bank, or banker or association, shall pay a tax of ten per centum on the amount of notes of any town, city or municipal corporation, paid out by them,' Veazie Bank *v.* Fenno was cited with approval to the point that congress, hav-

securities could be taxed. The majority of the court held that in so far as the Income Tax Act proposed to levy a tax upon the interest received by the holders of municipal bonds, as income, the act was repugnant also to the Constitution, and such tax

ing undertaken to provide a currency for the whole country, might, to secure the benefit of it to the people, restrain, by suitable enactments, the circulation as money of any notes not issued under its authority; and Mr. Chief Justice WAITE, speaking for the court, said: 'The tax thus laid is not on the obligation, but on its use in a particular way.' Scholey *v.* Rew, 23 Wall. 331, was a case of a succession tax which the court held to be plainly an excise tax or duty, upon the devolution of the estate or the right to become beneficially entitled to the same, or the income thereof, in possession or expectancy.' It was like the succession tax of a state held constitutional in Mager *v.* Grima, 8 How. 490; and the distinction between the power of a state and the power of the United States to regulate the succession of property was not referred to, and does not appear to have been in the mind of the court. The opinion stated that the act of parliament from which the particular provision under consideration was borrowed had received substantially the same construction, and cases under that act hold that a succession duty is not a tax upon income or upon property, but on the actual benefit derived by the individual determined as prescribed. In re Elwes, 3 H. & N. 719; Attorney-General *v.* Sefton, 2 H. & C. 362; s. c., (H. L.) 12 L. T. 242; 11 H. L. Cas. 257. In Railroad Company *v.* Collector, 100 U. S. 595, 596, the validity of a tax collected of a corporation upon the interest paid by it upon its bonds was held to be 'essentially an excise on the business of the class of corporations mentioned in the statute.' And Mr. Justice MILLER, in delivering the opinion, said: 'As the sum involved in this suit is small, and the law under which the tax in question was collected has long since been repealed, the case is of little consequence as regards any principle involved in it as a rule of future action.' All these cases are distinguishable from that in hand, and this brings us to consider that of Springer *v.* United States, 102 U. S. 586, 602, chiefly relied on and urged upon us as decisive. That was an action of ejectment brought on a tax deed issued to the United States on sale of defendant's real estate for income taxes. The defendant contended that the deed was void because the tax was a direct tax, not levied in accordance with the Constitution. Unless the tax were wholly invalid the defense failed. The statement of the case in the report shows that Springer returned a certain amount as his net income for the particular year, but does not give the details of what his income, gains and profits consisted in. The original record discloses that the balance was not derived in any degree from real estate, but was in part professional as attorney at law, and the rest interest on United States bonds. It would seem probable that the court did not feel called upon to advert to the distinction between the latter and the former source of income, as the validity of the tax as to either would sustain the action. The opinion thus concludes: 'Our conclusions are, that *direct taxes*, within the meaning of the Constitution, are only capitation taxes, as expressed in that instrument, and taxes on real estate,

would be invalid.[1] Upon a rehearing of this case the United States Supreme Court, by a majority, adhered to their former rulings, and their conclusions are those summed up by Mr. Chief Justice FULLER: First. "We adhere to the opinion already

and that the tax of which the plaintiff in error complains is within the category of an excise or duty.' While this language is broad enough to cover the interest as well as the professional earnings, the case would have been more significant as a precedent if the distinction had been brought out in the report and commented on in arriving at a judgment, for a tax on professional receipts might be treated as an excise or duty, and, therefore, indirect, when a tax on an income of personalty might be held to be direct."

[1] Pollock *v.* Farmers' Loan & Trust Co., (1895) 157 U. S. 429. Mr. Chief Justice FULLER, in delivering the opinion, said, upon the contention of the government: "We think the same want of power to tax the property or revenues of the states or their instrumentalities exists in relation to a tax on the income from their securities, and for the same reason, and that reason is given by Chief Justice MARSHALL in Weston *v.* Charleston, 2 Pet. 449, 468, where he said: 'The right to tax the contract to any extent, when made, must operate upon the power to borrow before it is exercised, and have a sensible influence on the contract. The extent of this influence depends on the will of a distinct government. To any extent, however inconsiderable, it is a burden on the operations of government. It may be carried to an extent which shall arrest them entirely. * * * The tax on government stock is thought by this court to be a tax on the contract, a tax on the power to borrow money on the credit of the United States, and consequently to be repugnant to the Constitution.' Applying this language to these municipal securities, it is obvious that taxation on the interest therefrom would operate on the power to borrow before it is exercised, and would have a sensible influence on the contract, and that the tax in question is a tax on the power of the states and their instrumentalities to borrow money, and consequently repugnant to the Constitution. Before this it had been said by the chief justice, *arguendo:* 'The Constitution contemplates the independent exercise by the nation and the state, and severally, of their constitutional powers. As the states cannot tax the powers, the operations, or the property of the United States, nor the means which they employ to carry their powers into execution, so it has been held that the United States have no power under the Constitution to tax either the instrumentalities or the property of a state. A municipal corporation is the representative of the state and one of the instrumentalities of the state government.' It was long ago determined that the property and revenues of municipal corporations are not subjects of federal taxation. Collector *v.* Day, 11 Wall. 113, 124; United States *v.* Railroad Company, 17 Wall. 322, 332. In Collector *v.* Day it was adjudged that congress had no power, even by an act taxing all incomes, to levy a tax upon the salaries of judicial officers of a state, for reasons similar to those on which it had been held in Dobbins *v.* Commissioners, 16 Pet. 435, that a state could not tax the salaries of officers of the United States. Mr. Justice NELSON, in delivering judgment, said: 'The general govern-

announced, that taxes on real estate being indisputably direct taxes, taxes on the rents or income of real estate are equally direct taxes. Second. We are of opinion that taxes on personal property, or on the income of personal property, are likewise direct taxes. Third. The tax imposed by sections twenty-seven to thirty-seven, inclusive, of the act of 1894, so far as it falls on income of real estate and of personal property, being a direct tax within the meaning of the Constitution, and, therefore, unconstitutional and void because not apportioned according to repre-

ment and the states, although both exist within the same territorial limits, are separate and distinct sovereignties, acting separately and independently of each other, within their respective spheres. The power in its appropriate sphere is supreme; but the states within the limits of their powers, not granted; or, in the language of the tenth amendment, 'reserved,' are as independent of the general government as that government within its sphere is independent of the states.' This is quoted in Van Brocklin *v.* Tennessee, 117 U. S. 151, 178, and the opinion continues: 'Applying the same principles, this court, in United States *v.* Railroad Company, 17 Wall. 322, held that a municipal corporation within a state could not be taxed by the United States on the dividends or interest of stock or bonds held by it in a railroad or canal company, because the municipal corporation was a representative of the state, created by the state to exercise a limited portion of its powers of government, and, therefore, its revenues, like those of the state itself, were not taxable by the United States. The revenues thus adjudged to be exempt from federal taxation were not themselves appropriated to any specific public use, nor derived from property held by the state or by the municipal corporation for any specific public use, but were part of the general income of that corporation, held for the public use in no other sense than all property and income, belonging to it in its municipal character, must be so held. The reasons for exempting all the property and income of a state, or of a municipal corporation, which is a political division of the state, from federal taxation, equally require the exemption of all the property and income of the national government from state taxation.' In Mercantile Bank *v.* New York, 121 U. S. 138, 162, this court said: 'Bonds issued by the state of New York, or under its authority by its public municipal bodies, are means of carrying on the work of the government, and are not taxable even by the United States, and it is not a part of the policy of the government which issues them to subject them to taxation for its own purposes.' The question in Bonaparte *v.* Tax Court, 104 U. S. 592, was whether the registered public debt of one state, exempt from taxation by that state, or actually taxed there, was taxable by another state when owned by a citizen of the latter, and it was held that there was no provision of the Constitution of the United States which prohibited such taxation. The states had not covenanted that this could not be done, whereas, under the fundamental law, as to the power to borrow money, neither the United States on the one hand, nor the states on the other, can interfere with that power, as possessed by each and an essential element of the sovereignty of each."

sentation, all those sections constituting one entire scheme of taxation, are necessarily invalid."[1]

§ 577. **Injunction of a collection of taxes.**— A railroad company, the property of which, by its acceptance of an act of the territorial legislature of North Dakota, was exempted until that act was repealed by the Constitution adopted when the territory became a state, it having paid the percentage of its gross earnings in lieu of the taxes for certain years as required by the act, sought in this case to restrain the officers of certain counties of the state from enforcing a tax upon its lands within those counties. The company having failed to make the payment for this particular year of the designated percentage of its gross earnings, or to make a tender of what was due under one or the other modes of taxation, the United States Supreme Court held that it was not entitled to relief in equity to enjoin the enforcement of a tax upon its property as upon the property of individuals in the counties in which the property was situated.[2]

[1] Pollock *v.* Farmers' Loan & Trust Co., (1895) 158 U. S. 601; Hyde v. Continental Trust Co., (1895) 158 U. S. 601.

[2] Northern Pacific R. R. Co. *v.* Clark, (1894) 153 U. S. 252. It was said by the court: "In State Railroad Tax Cases, 92 U. S. 575, 616, 617, the rule is established that before an injunction will be granted in such cases as the present, a party must pay or tender what can be seen to be due on the face of the bill; and speaking for the court in that case, Mr. Justice MILLER said that the duty of making such a tender or payment before any injunction will be allowed is laid down 'as a rule to govern the courts of the United States in their action in such cases.' This rule was repeated in National Bank *v.* Kimball, 103 U. S. 732, 733, where it was treated as a fatal objection to the bill that there was no offer to pay any sum as a tax which the party ought to pay; and, again, speaking for this court, Mr. Justice MILLER there said: 'We have announced more than once that it is the established rule of this court that no one can be permitted to go into a court of equity to enjoin the collection of a tax, until he has shown himself entitled to the aid of the court by paying so much of the tax assessed against him as it can be plainly seen he ought to pay,' etc."

CHAPTER XXXII.

TAXATION OF PRIVATE CORPORATIONS.

§ 578. General rules.
579. Exemption from taxation — rules.
580. Taxation of corporations — rules in New York.
581. Taxation of corporations — rules in Pennsylvania.
582. Privilege tax.
§ 583. Computation of such — rule.
584. Taxation of banks and shares of bank stock — rules.
585. Taxation of railroad corporations — rules.
586. Taxation of insurance corporations.

§ 578. **General rules.**— Stock in a railroad company built for use in its mining business, owned by a coal mining company, the railroad company having been already taxed upon its value, has been held not to be subject to tax as the property of the coal mining company.[1] A corporation having been taxed on its capital stock, the stock in the hands of its several owners is not liable to be retaxed again.[2] The charter of a New Jersey corporation exempting its property from the imposition of any tax or assessment, the Supreme Court of that state held exempted the corporation not only from taxation generally, but also from assessments for benefits derived from public improvements.[3] The

[1] Commonwealth *v.* Fall Brook Coal Co., 156 Pa. St. 488; s. c., 26 Atl. Rep. 1071.

[2] Commonwealth *v.* Lehigh Coal & Navigation Co., (Pa.) 29 Atl. Rep. 664. What is an essential part of the corporate property of a corporation chartered for transporting and storing oil and petroleum, etc., and not taxable, see Mellon Pipe Lines *v.* Allegheny County, 3 Pa. Dist. Rep. 448. For the rule under the statutes of Pennsylvania as to the appraisal of the capital stock of a corporation for taxation, see Commonwealth *v.* Pittsburg & W. R. Co., 166 Pa. St. 453; s. c., 31 Atl. Rep. 202; 36 W. N. C. 137; Commonwealth *v.* Edgerton Coal Co., 164 Pa. St. 284; s. c., 30 Atl. Rep. 125; 35 W. N. C. 205. How net earnings for the purpose of taxation should be ascertained, see Commonwealth *v.* Philadelphia & E. R. R. Co., 164 Pa. St. 252; s. c., 30 Atl. Rep. 145; 35 W. N. C. 217. For rule in ascertaining the net income of a corporation for taxation under Pennsylvania statutes, see Commonwealth *v.* Minersville Water Co., 2 Pa. Dist. Rep. 738. When stock of a corporation is "issued and outstanding" for the purpose of taxation under New Jersey statutes, see American Pig-Iron Storage Co. *v.* State Board of Assessors, (N. J.) 29 Atl. Rep. 160. When franchise of corporation is not taxable under New Jersey statutes, see Passaic Water Co. *v.* City of Paterson, (N. J.) 29 Atl. Rep. 185.

[3] Hudson County Catholic Protectory *v.* Board of Township Committee of Kearney, (N. J.) 28 Atl. Rep. 1043, following Protestant Foster Home

Nebraska Supreme Court has held that the constitutional provision in that state exempting property of religious corporations from general taxation did not exempt it from special assessments for local improvements.[1]

§ 579. **Exemption from taxation — rules.**— The power to exempt railroad corporations from taxation is within the scope of legislative power.[2] The grant of immunity to a railroad corporation from taxation, to be recognized, must be so plain as not to be mistaken.[3] The legislature of Tennessee, in the exercise of its power, in the act incorporating this railroad company, in the year 1848, provided for an exemption from taxation of the company in these words: "That the capital stock of said company shall be forever exempt from taxation, and the road, with all its fixtures and appurtenances, including workshops, warehouses and vehicles of transportation, shall be exempt from taxation for the period of twenty-five years from the completion of the road, and no tax shall ever be laid on said road or its fixtures which will reduce the dividends below eight per cent." The state, as well as several counties, after the expiration of the twenty-five years, assessed the road and fixtures of the company for taxation, and the State Supreme Court allowed these taxes which were declared liens upon the property of the company. The United

Soc. *v.* Mayor, etc., of Newark, 36 N. J. Law, 478.

[1] City of Beatrice *v.* Brethren Church, (Neb.) 59 N. W. Rep. 932. Rules relating to the exemption of property of manufacturing corporations under statutes or ordinances of municipal corporations for their encouragement, see Commonwealth *v.* Keystone Bridge Co., 156 Pa. St. 500; s. c., 27 Atl. Rep. 1; Commonwealth *v.* Pittsburgh Bridge Co., 156 Pa. St. 507; s. c., 27 Atl. Rep. 4; Commonwealth *v.* Thackara Mfg. Co., 156 Pa. St. 510; s. c., 27 Atl. Rep. 13; Commonwealth *v.* J. B. Lippincott Co., 156 Pa. St. 513; s. c., 27 Atl. Rep. 10, following Commonwealth *v.* Wm. Mann Co., 150 Pa. St. 64; s. c., 24 Atl. Rep. 601; Commonwealth *v.* Juniata Coke Co., 157 Pa. St. 507; s. c., 27 Atl. Rep. 373; Commonwealth *v.* Savage Fire Brick Co., 157 Pa. St. 512; s. c., 27 Atl. Rep. 374; 33 W. N. C. 136; Commonwealth *v.* Pottsville Iron & Steel Co., 157 Pa. St. 500; s. c., 27 Atl. Rep. 371; 33 W. N. C. 112; Commonwealth *v.* East Bangor Consolidated Slate Co., (Pa.) 29 Atl. Rep. 706; s. c., 34 W. N. C. 534. For a construction of the constitutional provision of Louisiana exempting property employed in manufacturing, see State *v.* Board of Assessors, (La.) 15 So. Rep. 384; Electric Traction & Mfg. Co. *v.* City of New Orleans, (La.) 14 So. Rep. 231.

[2] Neary *v.* Phil., Wil. & Balt. R. R. Co., (Del.) 9 Atl. Rep. 405.

[3] Chicago, B. & K. C. R. R. Co. *v.* Guffey, 122 U. S. 561; s. c., 7 Sup. Ct. Rep. 1300.

States Supreme Court held that it clearly had jurisdiction to review the decision of the State Supreme Court, in view of the fact that the exemption was within the constitutional power of the legislature to grant to the company, and was, therefore, a contract between the state and the company, and the state court had decided that the legislature did not violate or impair the obligation of any contract with the company.[1] Having determined that it had jurisdiction to review and revise the judgment of the State Supreme Court in this matter, the United States Supreme Court sustained the validity of the exemption, and the power of the legislature to exempt upon conditions or contingencies which were to happen in the future. They construed that portion of the act of incorporation which granted the exemption to have this effect: That the capital stock of the company is forever exempt from taxation during the existence of the corporation; the road and fixtures, etc., were exempt for twenty-five years after the completion of the road, which term had now expired; and now those portions of the property could be taxed only when the net earnings of the company were more than sufficient to pay to the stockholders, on the present basis of its capital, a dividend of eight per cent a year. But the court in sustaining the validity of the exemption did not mean to be understood as holding that the railroad company had the right, in its discretion, hereafter to issue additional stock, or to increase its bonded indebtedness, even for legitimate purposes, and have the same taken into consideration upon the question of its liability for taxation under the eight per cent dividend clause of the charter.[2] It appeared in this case that in the charter of a railroad company chartered in Missouri in 1857, there was a provision that its property should be exempt from taxation for a period of twenty years after its completion. Its road was completed in 1872. In 1870, under a general law of Missouri, it was consolidated with an Iowa corporation. In 1886 the consolidated road was sold under a decree of foreclosure of mortgage to purchasers who conveyed it to an Iowa corporation. The action was to charge the property in the hands of the purchaser company with a lien for state and county taxes levied on

[1] Mobile & Ohio R. R. Co. *v.* Tennessee, (1894) 153 U. S. 487.

[2] Mobile & Ohio R. R. Co. *v.* Tennessee, (1894) 153 U. S. 486. In this case the court discusses the questions of "dividends," "profits," "net profits" and what shall be deducted before the "net profits" can be determined quite at length, citing many cases.

the property of the former company in 1886. The question before the United States Supreme Court was whether the company succeeding the others by purchase at foreclosure was entitled to the exemption originally granted to the Missouri corporation in its charter. The court held that the consolidation of the Missouri corporation, under the general statute of that state, with the Iowa corporation, operated to extinguish the old company and to form a new one as of the date of the consolidation, and other provisions concerning exemption from taxation in the old charter did not pass to the new company.[1]

[1] Keokuk & Western R. R. Co. *v.* Missouri, (1894) 152 U. S. 301. As to the effect of consolidation of companies, see Tomlinson *v.* Branch, 15 Wall. 460; Philadelphia, etc., Railroad *v.* Maryland, 10 Hun, 376; Delaware Railroad Tax, 18 Wall. 206; Central Railroad *v.* Georgia, 92 U. S. 665; Chesapeake & Ohio Railroad *v.* Virginia, 94 U. S. 718; Green County *v.* Conness, 109 U. S. 104; Shields *v.* Ohio, 95 U. S. 319; Railroad Co. *v.* Maine, 96 U. S. 499; Railroad Co. *v.* Georgia, 98 U. S. 359, 362; St. Louis, Iron Mountain, etc., Railway *v.* Berry, 113 U. S. 465; McMahan *v.* Morrison, 16 Ind. 172; Memphis & Little Rock Railroad *v.* Commrs., 112 U. S. 609; Louisville & Nashville Railroad *v.* Palmes, 109 U. S. 244; Morgan *v.* Louisiana, 93 U. S. 217; Picard *v.* Tennessee, etc., Railroad, 130 U. S. 637; Tennessee *v.* Whitworth, 117 U. S. 139; Wilmington & Weldon Railroad *v.* Alsbrook, 146 U. S. 279, 297. As to exemptions, see Vicksburg & Meridian R. R. Co. *v.* Bradley, 66 Miss. 518; s. c., 6 So. Rep. 321; State *v.* Hannibal & St. Jo R. R. Co., (Mo.) 11 S. W. Rep. 746; Yazoo & M. V. R. R. Co. *v.* Board of Levee Comrs., 37 Fed. Rep. 24; Yazoo & M. V. R. R. Co. *v.* Thomas, 65 Miss. 553; s. c., 5 So. Rep. 108; State *v.* Keokuk & W. R. R. Co., 99 Mo. 30; s. c., 12 S. W. Rep. 290; Norwich & W. R. R. Co. *v.* County Commissioners, 151 Mass. 69; s. c., 23 N. E. Rep. 721; County of Stevens *v.* St. Paul, M. & M. Ry. Co., 36 Minn. 467; s. c., 31 N. W. Rep. 942; State *v.* Jersey City, (N. J.) 9 Atl. Rep. 782; Little Rock & Fort Smith Ry. *v.* Worthen, 120 U. S. 97; s. c., 7 Sup. Ct. Rep. 469; State *v.* Morris & Essex R. R. Co., (N. J.) 7 Atl. Rep. 826; Louisville & Nashville R. R. Co. *v.* Commonwealth, 89 Ky. 531; s. c., 12 S. W. Rep. 1064; Marye *v.* Baltimore & Ohio R. R. Co., 127 U. S. 117; s. c., 8 Sup. Ct. Rep. 1037; St. Paul, M. & M. Ry. Co. *v.* City of St. Paul, (Minn.) 38 N. W. Rep. 925; State *v.* Northern Pac. R. R. Co., 39 Minn. 25; s. c., 38 N. W. Rep. 635; Atlantic & P. R. R. Co. *v.* Lesueur (Ariz.) 19 Pac. Rep. 157; State *v.* Webber, (Minn.) 37 N. W. Rep. 949; Minnesota Cent. R. R. Co. *v.* Donaldson, 38 Minn. 115; s. c., 35 N. W. Rep. 725; Wisconsin Cent. R. R. Co. *v.* Comstock, 71 Wis. 88; s. c., 36 N. W. Rep. 843, following Railroad Company *v.* Price County, (Wis.) 26 N. W. Rep. 93. Exemption from taxation; when it does not pass to a purchaser at judicial sale, see Kentucky Central R. R. Co. *v.* Commonwealth, 87 Ky. 661; s. c., 10 S. W. Rep. 269; Pickard *v.* East Tennessee, Va. & Ga. R. R. Co., 130 U. S. 637; s. c., 9 Sup. Ct. Rep. 640; State *v.* Hannibal & St. Jo R. R. Co., (Mo.) 13 S. W. Rep. 505; Philadelphia, Wil. & Balt. R. R. Co. *v.* Neary, 5 Del. Ch. 600.

It has been held in Texas that the exemption from taxation by a statute, for good consideration, of property owned or to be owned by a railroad corporation or its successors, could not be withdrawn for failure to exercise corporate powers in the absence of a provision for forfeiture, as such exemption attached to the property.[1] In Mississippi, upon payment of a privilege tax, a railroad corporation is exempted from all state and county taxes except taxes on land owned by the corporation and not used in operating the road. Land owned by a railroad corporation separated by the track from the buildings of the road, not used for railroad purposes, and not necessary to its operation, has been held subject to taxation.[2] This railroad company was incorporated under an act of the North Carolina legislature with a capital stock of $3,000,000. The state subscribed for two-thirds of the shares and paid for them with six per cent bonds, the other shares being taken by private persons. By an act afterwards passed the charter of the company was amended so as to increase the capital stock to $4,000,000, the original amount being found to be insufficient to complete the road, and the state subscribed for the additional shares, paying for them with bonds as before. There was a provision in the act exempting from taxation all real estate held by the company for right of way, stations and workshops, until the dividends of profits should exceed six per cent per annum. A majority of the directors represented the state's interest. Under a tax law passed afterwards, the majority directors ordered the president to list all the property of the company for taxation. Certain shareholders filed a bill in the federal court to enjoin the president from such listing of the property. SIMONTON, Circuit Judge, held that the exemption provided for in the act amending the charter of the railroad company was a part of the contract between the state and the corporation, and that acts of the general assembly of North Carolina repealing that provision of the charter and providing for the listing of such property for taxation were void, as impairing the obligations of a contract.[3] It was held, therefore, that the majority of the board

[1] International & Great Northern Ry. Co. *v.* State, 75 Tex. 256; s. c., 12 S. W. Rep. 685.

[2] Lewis *v.* Vicksburg & Meridian R. R. Co., (Miss.) 6 So. Rep. 773.

[3] Barnes *v.* Kornegay, (1894) 62 Fed. Rep. 671. It was said: "The precise question arose in Tomlinson *v.* Jessup, 15 Wall. 458. A railroad company had obtained its charter and com-

of directors of this railroad company could not list for taxation the property exempted by the act amending the company's charter, against the protest of the minority stockholders.[1] And this majority of the directors representing the state having done everything they could as a board to surrender or destroy such exemption, in the face of the protest of the minority, and the governor and the state desiring such surrender, the bill of the minority stockholders was maintainable for the injunction prayed, without first going to the board of directors and endeavoring to induce them to prevent such taxation.[2] In a case before the United States Circuit Court for the eastern district of Louisiana, it appeared that by the charter of the bank which it was sought to collect taxes from by the state, the state had loaned several millions of dollars of its bonds to the bank, which bonds constituted the capital of the bank, were indorsed by it and sold. The stockholders were not immediately to pay anything upon their subscriptions, but were to furnish mortgages upon their plantations and slaves, which mortgages were to be held as security for payment of the lands and bear a certain interest. Certain duties were besides imposed upon the bank in the construction of certain public works to be afterwards turned over to the state. The profits were not distributable except to a limited amount until the payment of the bonds of the state was made. The stock, securities and profits of the bank were practically pledged for the

pleted its road under an act of the legislature containing no exemption from taxation. Some years afterwards it obtained an amendment to its charter, and in the amending act was the exemption. The state adopted a new Constitution, and in that Constitution it was sought to repeal all such exemptions. The Supreme Court of the United States, having these facts under consideration, says: 'In these cases, and in others of a similar character, the exemption is upheld as being made upon considerations moving to the state, which gives to the transaction the character of a contract. It is thus brought within the provisions of the Federal Constitution. In the case of a corporation, the exemption, if originally made in the act incorporating it, is supported upon the consideration of the duties and liabilities which the corporation assumes by accepting the charter. When made, as in the present case, by an amendment of the charter, it is supported upon the consideration of the greater efficiency with which the corporation will thus be enabled to discharge the duties originally assumed by the corporation to the public, or of the greater facility with which it will support its liability and carry out the purposes of its creation.'"

[1] Barnes *v.* Kornegay, (1894) 62 Fed. Rep. 671.

[2] Barnes *v.* Kornegay, (1894) 62 Fed. Rep. 671.

payment of the bonds. The act incorporating the bank exempted the capital of the bank from taxation "during the continuance of its charter." The court construed this exemption, as it was granted for the purpose of facilitating the repayment to the state of the capital advanced to the bank in the state's bonds, to continue not only for the duration of the bank's charter as then fixed, but for as long as the charter should exist as extended by the state at any future time, for the purpose of securing the repayment of such advances." and the charter having been extended in 1874, the exemption continued, notwithstanding the denial to the legislature by the Constitution of the state then in force of the power of exempting property from taxation, except such as was used for church, school or charitable purposes.[1] The legislature of Louisiana, in 1880, had passed an act authorizing this bank "to compromise and settle the liability of the mortgage stockholders of said bank arising out of the stock mortgages granted by them to secure their subscriptions to the capital stock of said bank, said compromises to be made when deemed judicious by said bank and with the assent of the bondholders," etc. The act also made provision "that all sums realized from said compromise, as well as from the enforcement of said mortgages by the usual legal proceedings, shall be held and applied by the banking department of said bank to the satisfaction of the bonds of the state, issued in aid of the bank, and to the legal liabilities of said mortgage stock department, and to the necessary expenses of said department." The tax officers in the case before the court claimed that the bank had waived its rights to exemption by assenting to the conditions included in the fourth section of this act which were to this effect: "That this act shall not be binding or confer any right upon the bank unless accepted within twelve months from the date of this act, and under the conditions prescribed in articles 234 and 237 of the Constitution. * * * " Article 234 is as follows: "The general assembly shall not remit the forfeiture of the charter of any corporation now existing, nor renew, alter or amend the same, nor pass any general or special law for the benefit of such corporation, except upon the condition that such

[1] Citizens' Bank of Louisiana *v.* Board of Assessors for the Parish of Orleans, (1893) 54 Fed. Rep. 73. The court in its argument upon this point refers to Tennessee *v.* Whitworth, 117 U. S. 145; s. c., 6 Sup. Ct. Rep. 649; Bank *v.* Bouny, 32 La. Ann. 245.

corporation shall hereafter hold its charter subject to the provisions of this Constitution." The court held that as it appeared that it would have been disastrous to the interests of the state to attempt to enforce those mortgages given by the stockholders, the act of the legislature authorizing a compromise of those oblitions was for the benefit of the state and ultimately to secure the payment of the bonds, and, therefore, not a privilege or favor granted to the bank, for the legislature had no authority to impose upon the bank the condition that its exemption from taxation should be thereafter waived; and though the bank intended, by acceptance of the act, to waive the exemption, the attempt to do so was of no effect, the capital of the bank being still exempt from taxation.[1] In this case a corporation which had been engaged in manufacturing in New Jersey, which had carried on business for a certain period, but afterwards ceased, the state having imposed a tax upon it because it was not engaged in the active business of manufacturing, claimed exemption under the statute passed in that state April 18, 1884.[2] The court held that, to bring itself within the immunity against taxation accorded by that statute to manufacturing corporations, the corporation must be actively engaged in the business of manufacturing.[3]

§ 580. **Taxation of corporations — rules in New York.**— In a case where a New Jersey corporation was assessed for taxation upon its moneys and property in the state of New York, it claimed that the amount of its debts should be deducted. The New York Court of Appeals held that foreign corporations were included within the statute of New York,[4] which provides as follows: "All persons and associations doing business in the state of New York as merchants, bankers or otherwise, either as principals or partners, whether special or otherwise, and not residents of this state, shall be assessed and taxed on all sums invested in

[1] Citizens' Bank of Louisiana *v.* Board of Assessors of the Parish of Orleans, (1893) 54 Fed. Rep. 73.

[2] Rev. Supp. N. J. 1017.

[3] State, Edison Phonograph Co., Prosecutor, *v.* State Board of Assessors, (1895) 55 N. J. L. 55; citing Construction Co. *v.* Board of Assessors, 53 N. J. L. 564. The court said: "A corporation wishing to withdraw from active business must, to escape taxation, take proceedings under the thirty-fourth section of the Corporation Act to dissolve and surrender its charter and wind up its affairs; but if it elects to continue its existence and retain its franchises, it must be subject to the tax which has been levied in this case (a tax upon its capital stock)."

[4] 1 N. Y. L. 1855, chap. 37.

any manner in said business the same as if they were residents of this state, and said taxes shall be collected from the property of the firms, persons or associations to which they severally belong."[1] As to the right to deduct debts it was said: "We are of the opinion that this act does not contemplate the deduction of debts from the sums invested in this state by non-residents. As the person is a non-resident, it is to be assumed that he will, at the place of his domicile, have all of what might be termed his equities adjusted, and that, if entitled to it anywhere, it will be at such domicile that he will claim and be allowed to have the right to have such deduction. In his case the statute of 1855 seizes upon the certain specific sum which he has here invested in the business carried on by him, and that sum is to be assessed and taxed the same as if the person were a resident of the state. In using the expression 'the same as if they were residents of this state,' we do not think it was intended that exceptions were to be allowed here the same as if the party were a resident, or that deductions from the sum thus invested should be made as if that were the case. It meant, as it seems to us, that the sum invested in any manner in business in this state should be assessed in the same manner and form as a resident would be assessed."[2] In this case the Court of Appeals of New York reversed the General Term of the Supreme Court, which affirmed the dismissal by the Special Term of a *certiorari* on the part of a manufacturing corporation to review an assessment of its property made by the commissioners of taxes and assessments of the city of New York. It appeared that the assessment was based solely upon statements of the corporation in answer to questions put by the commissioners, which statements showed that the capital of the corporation was impaired, and that the indebtedness of the company exceeded the value of its assets, exclusive of real estate, and did not disclose any fact or circumstance justifying a disbelief of the answer made, except that a dividend had been declared and paid shortly previous to the statement made. The court held that this statement as to a dividend having been declared did not authorize a disbelief in the statement of the impairment of capital, and, in the

[1] People ex rel. Thurber-Whyland Co. *v.* Barker, (1894) 141 N. Y. 118; citing British Com'l Life Ins. Co. *v.* Commrs. of Taxes, 1 Keyes, 303; cited in People ex rel. Bay State Shoe & Leather Co. *v.* McLean, 80 N. Y. 254, 259.

[2] People ex rel. Thurber-Whyland Co. *v.* Barker, (1894) 141 N. Y. 118, 121.

absence of any request on the part of the commissioners for further information, did not justify them in imposing a tax, as the statements, if accepted as true, showed that there was no basis for imposing the tax.[1] Under the provisions of the New York Corporation Tax Act,[2] giving to the state comptroller power to revise and adjust any account theretofore settled against a corporation for taxes arising under the act, and authorizing a review by *certiorari* of the action of the comptroller, relief may be given as provided where a tax has been imposed upon and paid by a corporation which was exempt from any taxation under the act. And the corporation will not be deprived of the relief granted by the statute by reason of the fact that the payment was not made under coercion.[3] Under New York statutes relative to the taxation of capital stock of corporations, the actual value and not the market value of its stock must be assessed.[4] The capital and surplus, and not the share stock, is the subject of valuation in assessing a corporation.[5] A corporation cannot be taxed upon stock of another corporation held by it, where the capital of the latter is taxable.[6] It is legal error to refuse to decide in accordance with evidence presented by a corporation to taxing officers as to the value of the corporation's assets, the evidence being so full and complete as to establish the basic facts upon which its claim for reduction of tax rests, it not being contradicted by facts within the knowledge of the taxing officers, and they having no good reason to doubt the truth of the evidence.[7] The indebtedness of a corporation should be deducted from the valuation of

[1] People ex rel. Edison General Electric Co. *v.* Barker, (1894) 141 N. Y. 251.

[2] N. Y. Laws, 1880, chap. 542; amended, N. Y. Laws, 1889, chap. 463.

[3] People ex rel. Edison Electric Illuminating Co. of New York *v.* Wemple, (1894) 141 N. Y. 471. See People, etc., *v.* Wemple, 133 N. Y. 617.

[4] People *v.* Barker, 146 N. Y. 304; s. c., 40 N. E. Rep. 996.

[5] United States Trust Co. *v.* Mayor, etc., of New York, 77 Hun, 182; s. c., 28 N. Y. Supp. 344; 59 N. Y. St. Repr. 496. See Trimmer *v.* City of Rochester, 130 N. Y. 401; People ex rel. Union Trust Co. *v.* Coleman, 126 N. Y. 433; National Bank of Chemung *v.* City of Elmira, 53 N. Y. 49; Re New York Catholic Protectory, 77 N. Y. 342; McLean *v.* Jephson, 123 N. Y. 143.

[6] People ex rel. Brooklyn Traction Co. *v.* Board of Assessors, 61 N. Y. St. Repr. 480; s. c., 30 N. Y. Supp. 448.

[7] People ex rel. German Looking Glass Plate Co. *v.* Barker, 75 Hun, 6; s. c., 26 N. Y. Supp. 971; 57 N. Y. St. Repr. 1. See People ex rel. Edison Electric Illuminating Co. *v.* Barker, 139 N. Y. 55.

its corporate assets in assessing its capital stock.[1] In assessing a corporation for taxation, the deduction of "non-taxable assets" has been held to be illegal.[2] There is no authority in the comptroller of the state of New York to impose a tax on real estate in the state, purchased by a corporation from its surplus as an investment, and not used in its business.[3] The capital of a domestic corporation of New York, invested in real estate in another state, in bonds of the United States deposited under a deed of trust in another state and in a foreign country with the minister of finance, to enable it to do business in the other state and foreign country, as required by the laws of the state and country, have been held not to be capital employed in the state of New York, subject to taxation, notwithstanding the fact that the interest upon the bonds was received and used in New York, and all the property was subject to the claims of all creditors of the corporation.[4] Property assessed for taxation may be released from the assessment by the legislature, its power over the subject being unlimited and exercisable in any way, and at any time before the taxes assessed are paid.[5] A special statute exempting the property of a corporation from local taxation, the exemption includes taxation from county as well as city purposes.[6] Foreign corporations have been held not to be entitled to a deduction of

[1] People ex rel. Second Avenue R. R. Co *v.* Barker, 141 N. Y. 196; s. c., 56 N. Y. St. Repr. 834.

[2] People ex rel. W. & J. Sloane *v.* Barker, 76 Hun, 454; s. c., 27 N. Y. Supp. 1082; 58 N. Y. St. Repr. 495. See People *v.* Ryan, 88 N. Y. 142.

[3] People ex rel. Singer Manufacturing Co. *v.* Wemple, 78 Hun, 63; s. c., 29 N. Y. Supp. 92; 60 N. Y. St. Repr. 662. See Williams *v.* Western Union Telegraph Co., 93 N. Y. 162; Burrall *v.* Bushwick R. R. Co., 75 N. Y. 211; Barry *v.* Merchants' Exchange Co., 1 Sandf. Ch. 280; Barclay *v.* Culver, 30 Hun, 1; People ex rel. Southern Cotton Oil Co. *v.* Wemple, 131 N. Y. 64; People *v.* American Bell Telephone Co., 117 N. Y. 241.

[4] People ex rel. American Surety Co. *v.* Campbell, 74 Hun, 101; s. c., 26 N. Y. Supp. 462. *Cf.* People *v.* New England Mut. Life Ins. Co., 26 N. Y. 303; People ex rel. Postal Telegraph Cable Co. *v.* Campbell, 24 N. Y. Supp. 208; People ex rel. American Contracting, etc., Co. *v.* Wemple, 129 N. Y. 558.

[5] People ex rel. American Bible Society *v.* Comrs. of Taxes & Assessments, 142 N. Y. 348. See Sisters of St. Francis *v.* Mayor, etc., of New York, 112 N. Y. 677; Association for Colored Orphans *v.* Mayor, etc., of New York, 104 N. Y. 581.

[6] People ex rel. Pratt Institute *v.* Board of Assessors of Brooklyn, 141 N. Y. 476. In 19 Abb. N. C. 231, will be found a note on the exemption of religious corporations from taxation. The statute of New York, Laws N. Y. 1892, chap. 399, § 2, in favor of religious corporations as to

their indebtedness, in the assessment of their property invested in business in the state of New York, though the indebtedness may be due within the state.[1]

§ 581. Taxation of corporations — rules in Pennsylvania. — Under the laws of Pennsylvania imposing a tax upon the indebtedness, as bonds, mortgages, etc., of corporations, the corporation is not liable for tax on so much of its indebtedness as may be held and owned by Pennsylvania corporations in their own right, or by persons not citizens of or residing in that state.[2] The statute making it the duty of the treasurer of the corporation to assess and retain and pay over to the state the tax imposed by the law under which these taxes were claimed upon indebtedness of the corporation on so much of indebtedness as was held by residents of that state, the corporation was held liable for his failure or neglect to do so.[3] Certain taxes were imposed upon a New York corporation, which had also been granted the privilege of constructing and operating a portion of its road through Pennsylvania, under the statute of Pennsylvania (P. L. Pa. 1885, 193, § 1), which assessed an annual tax of three mills on the dollar for state purposes, on all mortgages, money owing by solvent debtors, whether by promissory note or penal or single bill, bond or judgment, also all articles of agreement and accounts bearing interest, owned or possessed by any person or persons whatsoever (except notes or bills for work or labor done, and obligations given

exemptions from taxation applies only to corporations incorporated in the state of New York. Matter of Fayerweather, 31 Abb. N. C. 287; s. c., 30 N. Y. Supp. 273, following Matter of Prime, 136 N. Y. 347; Vanderpoel *v.* Gorman, 140 N. Y. 563, 575. As to the limit of the exemption of manufacturing corporations, foreign or domestic, doing business in the state of New York, see People ex rel. Tiffany & Co. *v.* Campbell, 80 Hun, 95; s. c., 30 N. Y. Supp. 70; 61 N. Y. St. Repr. 811, distinguishing People ex rel. Seth Thomas Clock Co. *v.* Wemple, 133 N. Y. 323; People *v.* Horn Silver Mining Co., 105 N. Y. 76. As to an exemption from taxation which was held erroneous, see Matter of Tiffany & Co., 80 Hun, 486; s. c., 30 N. Y. Supp. 494. When the exemption is not operative, see People ex rel. Western Electric Co. *v.* Campbell, 80 Hun, 466; s. c., 30 N. Y. Supp. 472.

[1] People *v.* Barker, 33 N. Y. Supp. 1019; People *v.* Barker, 86 Hun, 148; s. c., 33 N. Y. Supp. 221. As to the effect of voluntary payment of tax upon the right to recover it back, see United States Trust Co. *v.* Mayor, etc., of New York, 77 Hun, 182; s. c., 28 N. Y. Supp. 344; 59 N. Y. St. Repr. 496.

[2] Commonwealth *v.* Wilkesbarre & Scranton Railway Co., (1893) 14 Pa. Co. Ct. Rep., 205.

[3] Ibid.

to banks for money loaned and bank notes), on all public loans or stocks (except those issued by Pennsylvania or the United States), on all moneys loaned or invested in any other state and on all other moneyed capital in the hands of individual citizens of Pennsylvania, the property and interests so taxed being exempted from all taxation, except for state purposes, and the act not to apply to building or loan associations. Upon a writ of error from the Supreme Court of the State of Pennsylvania, which had affirmed the judgment of a lower court sustaining the taxes, the question presented to the Supreme Court of the United States was whether the commonwealth of Pennsylvania might, consistently with the Constitution of the United States, impose upon the railroad company the duty — when paying *in the city of New York* the interest due upon scrip, bonds or certificates of indebtedness held by residents of Pennsylvania — of deducting from the interest so paid the amount assessed upon bonds and moneyed capital in the hands of such residents of Pennsylvania. The court held that it could not. Also, that the section of that act making it "the duty of the treasurer of each private corporation, incorporated by or under the laws of this commonwealth, or the laws of any other state, or of the United States, and doing business in this commonwealth, upon the payment of any interest on any scrip, bond or certificate of indebtedness, issued by said corporation to residents of this commonwealth, and held by them, to assess the tax imposed and provided for state purposes upon the nominal value of each and every said evidence of debt, etc.," impaired the obligation of the contract originally made by the New York corporation and the state of Pennsylvania, as disclosed by those statutes, authorizing the construction of its road, etc., and by what was done by the companies, upon the faith of those acts.[1] When an insurance corporation of Pennsylvania, at the time of its dissolution by decree of the court, is a debtor to the state for tax on gross premiums, the debt continues to exist and is a charge on the assets passing into the hands of the receiver under the statute of 1876 of that state. And such a corporation is liable on the principle of apportionment only for the tax on the

[1] New York, L. E. & W. R. R. Co. *v.* Pennsylvania, (1894) 153 U. S. 628. The court did not consider State Tax on Foreign-held Bonds, 15 Wall. 300, 320, as controlling, and distinguished Bell's Gap Railroad Co. *v.* Pennsylvania, 134 U. S. 232; reaffirmed in Jennings *v.* Coal Ridge Improvement & Coal Co., 147 U. S. 147.

gross premiums received up to the time it is dissolved and not for the full six months.[1] One of the Courts of Common Pleas of Pennsylvania, in construing the Tax Act of that state of 1891, imposing taxes upon the capital stock of corporations, has declared the following rules: Only so much of the income of a corporation — whether called net earnings or amount of profit made — as is either declared in dividends or carried into surplus or sinking fund, is made the measure of the minimum price or value of the capital stock by the act referred to.[2] The amount of profit made, and either declared in dividends or carried into surplus or sinking fund, does not furnish an absolute measure of the actual value in cash of the capital stock of a corporation, but is to be considered, with all other pertinent facts, in determining what is its actual value in cash.[3]

§ 582. **Privilege tax.**— A franchise tax imposed upon a corporation as the price of the right and privilege of being a corporation, may be exacted by the state granting the franchise, no matter how the corporate property may be invested or employed, or where it may be situate.[4] Such a tax levied upon a manufacturing corporation of New Jersey was held not to be inconsistent with the terms of its charter which exempted from taxation "the real and personal property of the said corporation not actually in fact within the state of New Jersey, and the stock of the said corporation held or owned by any of its stockholders."[5] The

[1] Commonwealth *v.* American Life Insurance Co., (1893) 14 Pa. Co. Ct. Rep. 216. See, on the second ruling, Commonwealth *v.* Standard Oil Co., 101 Pa. St. 119; Commonwealth *v.* Pennsylvania Coal Co., 41 Leg. Int. 125; Commonwealth *v.* Western Union Telegraph Co., 15 W. N. C. 331; Pullman's Palace Car Co. *v.* Commonwealth, 107 Pa. St. 156; Commonwealth *v.* Canal Co., 50 Pa. St. 410; Commonwealth *v.* American Machine Co., 2 Ches. Co. 186.

[2] Commonwealth *v.* Edgerton Coal Co., (1893) 14 Pa. Co. Ct. Rep. 449, following Commonwealth *v.* Sharon Coal Co., Limited, (1893) 14 Pa. Co. Ct. Rep. 222. As to definitions of "net earnings" and "income," see Jones Mfg. Co. *v.* Commonwealth, 69 Pa. St. 137; Commonwealth *v.* Penn Gas Coal Co., 62 Pa. St. 241; Eyster *v.* Centennial Board of Finance, 94 U. S. 503.

[3] Commonwealth *v.* Edgerton Coal Co., (1893) 14 Pa. Co. Ct. Rep. 449.

[4] Honduras Commercial Company *v.* State Board of Assessors, (1892) 54 N. J. L. 278.

[5] The State, Singer Manufacturing Co., Prosecutor, *v.* Heppenheimer, (1892) 54 N. J. L. 439. The court said: "The question is evidently one of statutory construction in each case. Admit that an exemption of the company or its property, nothing else appearing, implies an exemption of the shares of its capital stock, and that

New Jersey Supreme Court on *certiorari* has upheld the yearly license fee imposed upon miscellaneous corporations imposed under the statute of April 18, 1884,[1] to which an objection was made that it was a levy upon interstate commerce, and, therefore, in violation of the Federal Constitution.[2] The United States

an exemption of the shares, nothing else appearing, implies an exemption of the company and its property, yet it is certainly within the power of the legislature to exempt the company or its property, and reserve the right to tax the company and its property. The corporation and the individual stockholders are obviously not included under the same description, nor are their rights identical (State *v.* Powers, 4 Zab. 400); both may be taxed, or either, as the legislature wills. State *v.* Branin, 3 Zab. 484. If, therefore, it appears by the charter of the prosecutor that the legislature in exempting the shares of its capital stock held or owned by individuals, did not mean to exempt the company or property, the decisions cited from 3 Zabriskie and 4 Zabriskie, become inapplicable, and the legislative purpose must prevail. Such a purpose is, I think, to be gathered from a consideration of all the provisions of the company's charter. In conjunction with the clause exempting the shares is an express exemption of the real and personal property of the corporation not actually within the state. Not only is this exemption superfluous, if the exemption of the shares was understood to relieve from taxation all the corporate property, but this express immunity conceded to property outside of the state affords the clearest implication that the taxability of corporate property within the state was to be preserved. Thus the implication which was countenanced in the former decisions is repelled by the statute now under review. The legislative intent, plainly embodied in this company's charter, is to relieve from taxation the shares of stock in the hands of its stockholders, but to reserve the right of levying upon the corporation itself any legal imposition except a tax on its real or personal property outside of New Jersey. The present tax, being levied upon the company for the exercise of its franchises within the state, comes under the reservation."

[1] N. J. Rev. Suppl. p. 1016.

[2] Lumberville Delaware Bridge Co. *v.* State Board of Assessors, (1893) 55 N. J. L. 529, citing in support of the holding, Robbins *v.* Shelby County, 120 U. S. 489; Leloup *v.* Mobile, 127 U. S. 648; The State Freight Tax, 15 Wall. 232; Railroad Co. *v.* Husen, 95 U. S. 465; Cook *v.* Pennsylvania, 97 U. S. 566; Brown *v.* Houston, 114 U. S. 622; Lyng *v.* Michigan, 135 U. S. 161; Norfolk & Western R. R. Co. *v.* Pennsylvania, 136 U. S. 115; Fargo *v.* Michigan, 121 U. S. 230; Crutcher *v.* Kentucky, 141 U. S. 47; Philadelphia St. Ship Co. *v.* Pennsylvania, 122 U. S. 326; Moran *v.* New Orleans, 112 U. S. 69; Pickard *v.* Pullman Southern Car Co., 117 U. S. 34; Pensacola Telegraph Co. *v.* Western Telegraph Co., 96 U. S. 1; Western Union Telegraph Co. *v.* Texas, 105 U. S. 460; Wabash, St. L. & Pac. Ry. Co. *v.* Illinois, 118 U. S. 557; Western Union Telegraph Co. *v.* Pendleton, 122 U. S. 347; Ratterman *v.* Western Union Telegraph Co., 127 U. S. 411; Wiggins Ferry Co. *v.* East St. Louis, 107 U. S. 365; Maine *v.* Grand Trunk Railway Co., 142 U. S. 217; Packet Co. *v.* Keokuk, 95 U. S. 80; Packet Co. *v.* St. Louis, 100 U. S. 428; Packet Co. *v.* Catlettsburg, 105 U. S. 563; Transportation Co. *v.* Par-

Supreme Court considered a statute of Ohio, under which there was imposed upon a railroad company a fee to the state, and held that if several railroad corporations, each existing under the laws of separate states, consolidate into one corporation, the statute of one of the states imposing a charge upon the new consolidated company of a percentage on its entire authorized stock as the fee to the state for the filing of the articles of consolidation in the office of the secretary of state, without which filing it could not possess the powers, immunities and privileges which appertain to a corporation in that state, was not a tax on interstate commerce, or the right to carry on the same, or the instruments thereof; and that its enforcement involved no attempt on the part of the state to extend its taxing power beyond its territorial limits.[1]

kersburg, 107 U. S. 698; Ouachita Packet Co. *v.* Aiken, 121 U. S. 444; Coe *v.* Errol, 116 U. S. 517; Western Union Telegraph Co. *v.* Massachusetts, 125 U. S. 530; Pullman Palace Car *v.* Pennsylvania, 141 U. S. 18; Delaware Railroad Tax Case, 18 Wall. 206; Horn Silver Mining Co. *v.* New York, 143 U. S. 305; Minot *v.* Philadelphia, Wilmington & Baltimore R. R. Co., 18 Wall. 206; State Tax on Railway Gross Receipts, 15 Wall. 284. The New Jersey court said: "The franchise that is taxed as property is the privilege enjoyed by a corporation of exercising certain powers derived from the state, whereas the franchise with which we have to do is the right to exist in corporate form without reference to the powers that under such form the company may exercise. This distinction, although formulated by Mr. Justice FIELD in Home Insurance Co. *v.* New York, 134 U. S. 594, was not strictly adhered to in his subsequent expressions, probably because there was nothing in that case to call for a nice use of terms. In this state we tax each of these so-called franchises. The power, as in the case of the right to own and operate a railroad is taxed as property having a true value, which it is the duty of the state board to ascertain for the purposes of constitutional assessment. On the other hand, the naked right of existing in corporate forms is taxed as in the case before us, not at its true value, as it would have to be if it were property, but at a sum arbitrarily imposed by the legislature as an annual fee, the amount of which is to be computed by reference to the capital of the company as a criterion. It is, in short, a poll tax levied upon domestic corporations for the right to be. Such a tax is not upon property or assets and does not in any way concern the nature of the business the company may be authorized to carry on. If the business chance to be one of commercial intercourse with other states, the burden incidental to corporate existence does not, under the federal decisions [already] cited, constitute a regulation of that commerce."

[1] Ashley *v.* Ryan, (1894) 153 U. S. 436. The court said: "As it was within the discretion of the state to withhold or grant the privilege of exercising corporate existence, it was, as a necessary resultant, also within its power to impose whatever conditions it might deem fit as prerequisite to corporate life. The act of filing, constituting, as it did, a claim of a

§ 583. Computation of such tax — rule.— There was also an objection in this case to the manner of computing the tax, the contention being that inasmuch as the erection of the bridge was a joint enterprise requiring the concurrent legislation of two states, the capital to be taken as the criterion of the license fee should be one-half of the capital the domestic corporation was authorized to have. The court sustained the mode of computing the tax upon the total capital of the corporation.[1]

§ 584. Taxation of banks and shares of bank stock — rules.— On *certiorari* the Supreme Court of New Jersey set aside taxes imposed upon shares of stock held by the prosecutor in a foreign corporation, having its principal place of business in

right to the franchise granted by the state law, carried with it a voluntary assumption of any burden with which the privilege was accompanied, and without which the right to corporate existence could not have been procured. We say *voluntary* assumption, because, as the claim to the franchise was voluntary, the assumption of the privilege which resulted from it partook necessarily of the nature of the claim for corporate existence. Having thus accepted the act of grace of the state, and taken the advantages which spring from it, the company cannot be permitted to hold on to the privilege or rights granted and at the same time repudiate the condition by the performance of which it could alone obtain the privilege which it sought."

[1] Lumberville Delaware Bridge Co. *v.* State Board of Assessors, (1893) 55 N. J. L. 529. The court, referring to Easton Delaware Bridge Co. *v.* Metz, Collector, 32 N. J. L. 199, which suggested the contention, said: "That case has, however, no application. The tax there considered was imposed directly upon the capital and surplus which, so the court held, was intended by the legislature to embrace one-half of an enterprise resting in dual legislation. Since the last amendments of the Constitution such a tax is a legal impossibility, and the construction placed by the court upon the legislative intent with respect to the amount of property to be embraced in the tax is no aid in the present case, where the tax is not upon capital or property put to the common use of a domestic and a foreign organization, but is the price the domestic company must pay for the right of corporate life. Such a right is in its nature indivisible, and the fee, therefore, must necessarily be an entirety. In computing such a fee the board of assessors has no discretion — the legislative mandate is plain and cannot be departed from by the assessors nor modified by the courts. In The Evening Journal Association *v.* The State Board of Assessors, 47 N. J. L. 36, the business in which the capital of the corporation was invested was considered by this court for the purpose of determining whether it was a "manufacturing company" within the meaning of the statute. And in The Press Printing Company *v.* The State Board of Assessors, 51 N. J. L. 75, the court, finding that the corporation was in one sense and as to a distinct part of its capital a manufacturing company, adopted as the criterion for the ascertainment of the amount of

another state, it appearing that taxes had been actually assessed in the other state, and paid by the corporation, within twelve months before the day prescribed by law for commencing the assessment of taxes in New Jersey, holding them exempt from taxation in that state. They also set aside the taxes imposed upon his shares of stock in a national banking association located in another state, holding that they could not be taxed under the laws of New Jersey.[1] The laws of Washington, providing for the assessment of bank stock for taxes, make bankers the agents for their respective shareholders, and authorize the collection from each bank of taxes upon its stock as assessed against it as such agent. The assessments upon the stock or shares of the shareholders in this case were assessed separately against each shareholder. The bank was not charged upon the assessment roll as agent for its shareholders, nor charged at all for any tax upon its stock, nor even referred to by its proper corporate name in the assessments against its several shareholders. The bank brought this suit against the treasurer of the county to restrain the collection of the tax from the bank. The United States Circuit Court overruled a demurrer to the bill, holding that under the above state-

the tax which, under the act of 1881 (Rev. Supp. p. 602), the court was required to impose, the capital of the corporation not within the exemption. In the present case no such questions arise."

[1] The State, De Baun, Prosecutor, *v.* Smith, Collector of Washington Township, (1892) 55 N. J. L. 110. Upon this last ruling it was said: "The federal statute for the organization of banking associations permits shares in them to be taxed under authority of the state within which the bank is located, and expressly provides that shares owned by non-residents of the state may be taxed in the city or town where the bank is located, and not elsewhere. This statute, by fair construction, excludes all state taxation of the shares of stock except such as it expressly permits, and this exclusion is constitutional and valid. Van Allen *v.* The Assessors, 3 Wall. 573; North Ward National Bank *v.* City of Newark, 39 N. J. L. 380. Consequently shares of stock in a national banking association cannot be taxed by any state except that within which the bank is located; they are withdrawn from taxation under the authority of other states. Tappan *v.* Merchants' National Bank, 19 Wall. 490." Upon the first ruling, see The State, Smith, Prosecutor, *v.* Ramsey, Collector, etc., (1892) 54 N. J. L. 546. As to the right of a state to tax shares of stockholders in national banking associations within its limits, see Van Slyke *v.* Wisconsin, (1871) 154 U. S. 581, following National Bank *v.* Commonwealth, 9 Wall. 353; Lionberger *v.* Rouse, 9 Wall. 468. As to the state's power to legislate as to taxation of bank shares and fix the situs of the stock for purposes of taxation, see Stockholders of Bank of Abingdon *v.* Supervisors of Washington County, (1891) 88 Va. 293; Tappan *v.* Merchants' National Bank, 19 Wall. 490.

ment of facts the warrant to the collector conferred no authority upon him to seize the property of the bank for the purpose of enforcing payment of the taxes charged against the individual shareholders; neither did the law authorize the bank to pay said taxes, and charge the same to the shareholders. The court also said: "Unjust discrimination in the valuation of national bank stock, as compared with the assessment of other moneyed capital in the hands of individual citizens of the state, is prohibited.[1] Nor did the failure of the bank to make and keep good a tender of so much of the tax as was justly due bar such relief, where nothing was due from the bank, there being no assessment against it, and the county officers having declared that they would not accept less than the whole amount levied.[2] Shareholders of national bank stock have this statute as a guaranty that they cannot be taxed upon their stock heavier than other moneyed capital in the state; and when appealed to in their behalf, the courts are bound to give effect to the law. If inequality is shown to the prejudice of shareholders, either the assessment must be declared to be entirely void, or at least the excess of the tax above the rate imposed upon other moneyed capital must be abrogated.[3] A court of equity is the proper forum to grant relief, and an injunction is the proper remedy."[4] It was also held that failure to exhaust the means of redress afforded by the laws of Washington for equalization of assessments did not preclude a national bank from obtaining relief in a federal court in the state, against the collection from it of taxes on its stock, on the ground of unjust discrimination in the valuation of such stock.[5] A portion of the capital stock of a national bank in Iowa being invested in real estate, and such real estate being assessed for taxation, the Supreme Court of that state held that the stock of the bank could be taxed to the extent only of such proportion of its market value as might remain after deducting therefrom the actual value of the real estate.[6] It was also held by the Supreme Court in this

[1] Rev. St. U. S. § 5219.

[2] First Nat. Bank of Walla Walla *v.* Hungate, (1894) 62 Fed. Rep. 548.

[3] Citing People *v.* Weaver, 100 U. S. 539; Pelton *v.* Bank, 101 U. S. 143; Cummings *v.* Bank, 101 U. S. 153; Boyer *v.* Boyer, 113 U. S. 689; s. c., 5 Sup. Ct. Rep. 706; Puget Sound Nat. Bank *v.* King Co., 57 Fed. Rep. 433.

[4] First Nat. Bank of Walla Walla *v.* Hungate, (1894) 62 Fed. Rep. 548.

[5] First Nat. Bank of Walla Walla *v.* Hungate, (1894) 62 Fed. Rep. 548; Andrews *v.* King Co., 1 Wash. St. 46; s. c., 23 Pac. Rep. 409, followed.

[6] First National Bank of Albia *v.* City Council of Albia, (1892) 86 Iowa, 28. It was said in the opinion of the

case, which was a tax imposed upon shares in the stock of a national bank, that the shares were credits within the meaning of the Code of Iowa, section 814, entitling a taxpayer to deduct, from the gross amount of his credits listed for taxation, all debts owing to him in good faith.[1] Shares of stockholders in national banking

court: "Section 5219 of the federal statutes authorizes the states to tax these banks, and contains the restriction 'that the taxation shall not be at a greater rate than is assessed on other moneyed capital in the hands of individual citizens of such state.' The same statute authorizes the taxation of the real estate held by such banks 'to the same extent, according to its value, as other real estate is taxed.' It is said in National State Bank *v.* Young, 25 Iowa, 311, 314: 'The shares of the stockholders represent the capital of the institution. To tax the shares and also the property of the bank would be double taxation.' People *v.* Weaver, 100 U. S. 539; 1 Desty on Taxation, pp. 199, 200, 379, 383. See, also, Tallman *v.* Treasurer of Butler Co., 12 Iowa, 531, where the court said: 'The shares of stockholders are theoretically, if not practically, measured in value by the property of the corporation. * * * However held [the lands], whether in fee or otherwise by the company, they are a part of the capital — affect the value of the stock which is taxable through the shares. To tax the land and the stock also which represents it, and which is enhanced by the value of the land, it seems to us would be double taxation.' In the case of In re Appeal of Des Moines Water Co., 48 Iowa, 324, 333, it is held the stock of a corporation must be taxed as the property of the corporation owners, and the question as to whether both the shares and the corporate property shall be taxed at the same time was not determined. In Cook *v.* City of Burlington, 59 Iowa, 251, the case last cited is approved, and a majority of the court held that the property of a corporation may be taxed, and that, at the same time, the stock can be taxed to the individual owners; and after citing Tallman *v.* Treasurer of Butler Co., 12 Iowa, 534; United States Express Co. *v.* Ellyson, 28 Iowa, 370, 378; McGregor's Exrs. *v.* Vanpel, 24 Iowa, 436, the court further says that it has never held 'that what is denominated 'duplicate taxation' is in excess of the legislative power. The most that can be said of these utterances of the courts is that it should be held in disfavor by courts and legislatures.' In Henkle *v.* Town of Keota, 68 Iowa, 338, the doctrine announced in Des Moines Water Co.'s Appeal and Cook *v.* City of Burlington is approved, and it is expressly held that shares of stock in a bank incorporated under the state law were taxable to the shareholders." The court cited in support of the ruling in the text People *v.* Weaver, 100 U. S. 539; Supervisors *v.* Stanley, 105 U. S. 305; 1 Desty on Taxation, 383.

[1] First National Bank of Albia *v.* City Council of Albia, (1892) 86 Iowa, 28. The court said: "In Equitable Life Ins. Co. *v.* Board of Equalization, 74 Iowa, 181, it was held that among the debts of the plaintiff to its stockholders was the amount which they would be entitled to recover upon a present distribution of the assets of the company. These assets clearly must include the stock, and, hence, if it be treated as a debt owing by the corporation to its stockholders, or which would be due to them if the business of the company was to be wound up,

associations within the limits of a state are subject to taxation by the state.[1] But a state cannot tax national bank stock in excess of other moneyed capital of its citizens, as by refusing to deduct the excess of its debts over credits of the stockholders from the amount of their stock.[2] Under the statutes of New York, with reference to taxation of shares of stock of banks, it has been held that an assessment of bank stock in the name of the person appearing on the list furnished the tax officers by the officers of the bank was valid as against the real owner, to whom the shares were transferred before the assessment was made, the assessment in the name of the person appearing on the list as owner being, in effect, an assessment on the shares, against whoever owned them at the time of the assessment.[3] A shareholder in a banking corporation, it has been held in Missouri, is not liable for taxes assessed against the property of the bank under the statutes of that state.[4] The statute of Iowa provides for the taxation of shares of bank stock, and requires the officers to furnish the assessors "the name of each person owning shares, and the amount owned by each." Under that statute an assessment on the capital stock as the personal property of the bank, without mention of the shareholders, has been held to be void.[5] The statute of North Carolina requires the officers of a corporation to list for taxation all the "shares of stock" held therein and the value thereof. It has been held that under this statute the capital stock must be

and its assets distributed to those entitled thereto, it would seem to us to follow that, as to the stockholders, the stock which they hold must at least, so far as the matter of taxation is concerned, be treated and considered as 'credits.' * * * If, as is clearly held in this case, the obligation of the corporation to repay the stockholder the amount paid for the stock is a 'debt' of the corporation to the stockholder, it is certain that as to him for taxation purposes, at least, it must be treated as a 'credit.' See, also, Hawkeye Ins. Co. *v.* Board of Equalization, 75 Iowa, 770, where the doctrine announced above is followed and approved."

[1] Van Slyke *v.* State of Wisconsin, 154 U. S. 581; s. c., 14 Sup. Ct. Rep. 1168; Bagnall *v.* State of Wisconsin, ibid. See Adair *v.* Robinson, 6 Tex. Civ. App. 275; Niles *v.* Shaw, 50 Ohio St. 370.

[2] First National Bank *v.* Chapman, 9 Ohio Cir. Ct. Rep. 79.

[3] People *v.* Barker, 87 Hun, 194; s. c., 33 N. Y. Supp. 1042. For an illustration of an assessment upon the stock of a national bank which was held to be illegal, see People ex rel. Sheldon *v.* Fraser, 74 Hun, 282; s. c., 26 N. Y. Supp. 814; 56 N. Y. St. Repr. 888.

[4] State *v.* Catron, 118 Mo. 280; s. c., 24 S. W. Rep. 439.

[5] Farmers & Traders' Nat. Bank *v.* Hoffmann, (Iowa) 61 N. W. Rep. 418.

listed by the officers of the corporation and not by individual stockholders.[1]

§ 585. **Taxation of railroad corporations — rules.** — A provision in the charter of a railroad corporation that it should pay to the state a fixed sum as taxes, "and no more," has been held not to relieve it from county taxation.[2] For the purpose of county taxation the roadbed of a railroad company constitutes "real property."[3] The term "capital stock" in the tax law of Kentucky has been held to include the entire property, real and personal, tangible and intangible, as well as the value of the franchise.[4] Where rolling stock is constantly changing the amount for taxation may be fixed by the average amount of the rolling stock used upon a road.[5] The part of a tax paid by a railroad company which has been illegally collected of it, should be applied to valid taxes subsequently accruing against it.[6] A tax upon a railroad corporation which has purchased a railroad, aided by a subscription of a county, for the purpose of meeting that subscription, is limited to the improvements made upon the road after its purchase.[7] A hotel owned by a railroad corporation, leased by it for a summer resort, has been held not to come within the ordinary exemption of the railroad corporation from taxation in Minnesota.[8] The United States Supreme Court has held that the act

[1] Charlotte Building & Loan Association *v.* Board Comrs. Mecklenburg County, 115 N. C. 410; s. c., 20 S. E. Rep. 526. As to taxation of shares of stock in banks, and statements required of the banks in connection therewith, see First Nat. Bank *v.* Bailey, (Mont.) 39 Pac. Rep. 83; Eaton *v.* Union County Nat. Bank, 40 N. E. Rep. 668.

[2] Kentucky Central R. R. Co. *v.* County of Pendleton, (Ky.) 2 S. W. Rep. 176.

[3] Neary *v.* Philadelphia, Wilmington & Baltimore R. R. Co., (Del.) 9 Atl. Rep. 405.

[4] Henderson Bridge Company *v.* Commonwealth, (Ky.) 31 S. W. Rep. 486. What is not double taxation on property of a corporation, see Pacific Coast Ry. Co. *v.* Ramage, (Cal.) 37 Pac. Rep. 532; United States Electric Power & Light Co. *v.* State, 79 Md. 63; State *v.* Bank of Commerce, (Tenn.) 31 S. W. Rep. 993.

[5] Atlantic & Pac. R. R. Co. *v.* Le Sueur, (Ariz.) 19 Pac. Rep. 157.

[6] Northern Pacific R. R. Co. *v.* Raymond, (Dak.) 40 N. W. Rep. 538; State *v.* Missouri Pac. Ry. Co., (Mo.) 6 S. W. Rep. 862. See, also, Boston, C. & M. R. R. Co. *v.* State, 64 N. H. 490; s. c., 13 Atl. Rep. 874.

[7] Louisville & Nashville R. R. Co. *v.* Hopkins County, 87 Ky. 605; s. c., 9 S. W. Rep. 497.

[8] County of Hennepin *v.* St. Paul, M. & M. Ry. Co., 42 Minn. 238; s. c., 44 N. W. Rep. 63. Cases in which the statutes for taxing railroads have been held to be unconstitutional: Central Railroad *v.* State Board of As-

of the legislature of Indiana of March 6, 1891, concerning taxation, under the provisions of which there was an assessment upon the railroad company's property by the state board of assessors, not to be obnoxious to the constitutional objections made to it on the hearing, as the Supreme Court of Indiana had decided that the Constitution of that state authorized such a method of assessing railroad property, which decision was binding upon the United States Supreme Court. Further, the act gives the railroad companies the right to be heard before final determination of the question, which construction was also conclusive upon this court. Further than this, a tax law which grants to the taxpayer a right to be heard on the assessment of his property before final judgment,

sessors, 49 N. J. L. 1; s. c., 7 Atl. Rep. 306. Where they were held to be constitutional: Owensboro & N. Ry. Co. *v.* County of Daviess, (Ky.) 3 S. W. Rep. 164. Taxation on "undivided profits" for a railroad company under federal statute construed: Marquette, H. & O. R. R. Co. *v.* United States, 123 U. S. 722; s. c., 8 Sup. Ct. Rep. 319. Taxation upon earnings of a railroad corporation; rules as to computation of, etc.: State *v.* Northern Pacific R. R. Co., 36 Minn. 207; s. c., 30 N. W. Rep. 663. What is taxable property of a railroad corporation: City of Muscatine *v.* Chicago, R. I. & P. Ry. Co., 79 Iowa, 645; s. c., 44 N. W. Rep. 909; Nashua & Lowell Railroad *v.* City of Nashua, 62 N. H. 602; Boston, C. & M. Railroad *v.* State, 62 N. H. 648. Assessment of railroad property for taxation; rules for ascertaining value: People *v.* Hicks, 105 N. Y. 198; s. c., 11 N. E. Rep. 653; Central Railroad *v.* State Board of Assessors, 49 N. J. L. 1; s. c., 7 Atl. Rep. 306; Ohio & Mississippi Ry. Co. *v.* People, 120 Ill. 200; s. c., 10 N. E. Rep. 545; People *v.* Comrs. of Taxes, 104 N. Y. 240; s. c., 10 N. E. Rep. 437; People *v.* Assessor, 2 N. Y. Supp. 240; State *v.* Union Trust Co., (Mo.) 6 S. W. Rep. 867; Morgan's La. & Tex. R. R. & St. Ship Co. *v.* Board of Reviewers, (La.) 3 So. Rep. 507. Rule as to computing the length of a railroad: Herbert *v.* Baltimore & Philadelphia R. R. Co., (Del.) 13 Atl. Rep. 902; State *v.* Nashville, C. & St. L. R. R. Co., 2 Pickle, 438; s. c., (Tenn.) 6 S. W. Rep. 880; State Board of Assessors *v.* Paterson & R. R. R. Co., 50 N. J. L. 446; s. c., 14 Atl. Rep. 610; Todd County *v.* St. Paul, M. & M. Ry. Co., (Minn.) 36 N. W. Rep. 109. Assessment for back taxes; rules governing: State *v.* Hannibal & St. Jo R. R. Co., (Mo.) 11 S. W. Rep. 746; State *v.* Wabash, St. L. & Pac. Ry. Co., 97 Mo. 296; s. c., 10 S. W. Rep. 434. When unauthorized: Franklin County Court *v.* Louisville & Nashville R. R. Co., 84 Ky. 59. Where and by whom assessments of taxation on railroad companies should be made: Oregon Short Line Ry. Co. *v.* Yeates, (Idaho) 17 Pac. Rep. 457; Morgan's La. & Tex. R. R. & St. Ship Co. *v.* Board of Reviewers, (La.) 3 So. Rep. 507; Missouri Valley & B. Ry. & B. Co. *v.* Harrison County, 74 Iowa, 283; s. c., 37 N. W. Rep. 372. Assessment of tax, upon railroad property, in New Hampshire, see Boston C. & M. Railroad *v.* State, 62 N. H. 648. Assessment upon railroad track in Illinois; not to be assessed by local assessor, see Chicago & A. R. R. Co.

provides a due process of law for determining the valuation, although it makes no provision for a rehearing.[1] An assessment made upon a railroad company's property in Indiana was objected to on the ground that it was based partly upon property outside of the state, the road running also through the adjoining state. The United States Supreme Court, after a consideration of the questions made, determined as follows: If an assessing board, seeking to assess for purposes of taxation a part of a railroad within a state, the other part of which is in an adjoining state,

v. People, 129 Ill. 571; s. c., 22 N. E. Rep. 864. When corporation is estopped to complain of assessment by town assessor, see Indianapolis & St. Louis Ry. Co. *v.* People, 130 Ill. 62; s. c., 22 N. E. Rep. 854. In Nebraska, see Red Willow County *v.* Chicago, B. & Q. Railroad Company, 26 Neb. 660; s. c., 42 N. W. Rep. 879. In New Jersey, see Williams *v.* State Board of Assessors, 51 N. J. Law, 512; s. c., 18 Atl. Rep. 750. In Iowa, see Missouri Valley & B. Ry. & B. Co. *v.* Harrison County, 74 Iowa, 283. In Kentucky, see Louisville & N. R. R. Co. *v.* Commonwealth, 85 Ky. 198. In Tennessee, see Shelby County *v.* Mississippi & T. R. Co., 16 Lea, 401; s. c., 1 S. W. Rep. 32. In Missouri, see State *v.* Hannibal & St. Jo R. R. Co., (Mo.) 13 S. W. Rep. 505. In New York, see People *v.* Cheetham, 45 Hun, 6; s. c., 20 Abb. N. C. 44; Atlantic & P. Ry. Co. *v.* Yavapai County, (Ariz.) 21 Pac. Rep. 768. The right to attack a valuation of its property, see St. Louis Bridge & Tunnel R. R. Co. *v.* People, 127 Ill. 627; s. c., 21 N. E. Rep. 348, following Railway Co. *v.* People, 10 N. E. Rep. 397. Rule of valuation in Kentucky, see Owensboro & N. Ry. Co. *v.* Logan County, (Ky.) 11 S. W. Rep. 76. As established by earning capacity, see People *v.* Haren, 3 N. Y. Supp. 86. When a railroad bridge must be assessed with the railroad, see State *v.* Hannibal & St. Jo. R. R. Co., 97 Mo. 348; s. c., 10 S. W. Rep. 436. When an assessment is void, see St. Louis & S. F. Ry. Co. *v.* Apperson, 97 Mo. 300; s. c., 10 S. W. Rep. 478; State of California *v.* Central Pacific R. R. Co., 127 U. S. 1; s. c., 8 Sup. Ct. Rep. 1073. Return of miles of railroad in Nebraska for taxation: Cass County *v.* Chicago, B. & Q. R. R. Co., 25 Neb. 348; s. c., 41 N. W. Rep. 246; Chicago, B. & Q. R. R. Co. *v.* School District No. 1, 25 Neb. 359; s. c., 41 N. W. Rep. 249. Taxation of lands granted to railroads; rules: State *v.* Central Pacific R. R. Co., (Nev.) 22 Pac. Rep. 237; St. Paul & Sioux City R. R. Co. *v.* Robinson, 40 Minn. 367; s. c., 43 N. W. Rep. 75; St. Paul & Sioux City R. R. Co. *v.* Shanks, 40 Minn. 369; s. c., 42 N. W. Rep. 83; Sioux City & St. Paul R. R. Co. *v.* Robinson, 41 Minn. 452; s. c., 43 N. W. Rep. 326; Sioux City & St. Paul R. R. Co. *v.* King, 41 Minn. 461; s. c., 43 N. W. Rep. 329. Taxation of railroads for school purposes in Missouri: Chicago & A. R. R. Co. *v.* Lamkin, 97 Mo. 496; s. c., 10 S. W. Rep. 200. Taxation of foreign railroad corporations running into Pennsylvania: Commonwealth *v.* Lehigh Valley R. R. Co., (Pa.) 17 Atl. Rep. 179; Delaware & Hudson Canal Co. *v.* Commonwealth, (Pa.) 17 Atl. Rep. 175.

[1] Pittsburgh, Cincinnati, Chicago & St. Louis Ry. Co. *v.* Backus, (1894) 154 U. S. 421.

ascertains the value of the whole line as a single property, and then determines the value of that within the state upon the mileage basis, that is not a valuation of property outside of the state; and the assessing board, in order to keep within the limits of state jurisdiction, need not treat the part of the road within the state as an independent line, disconnected from the part without, and place upon that property only the value which can be given to it if operated separately from the balance of the road. Where an assessing board is charged with the duty of valuing a certain number of miles of railroad within a state forming part of a line of road running into another state, and assesses those miles of road at their actual cost value, determined on a mileage basis, this does not place a burden upon interstate commerce beyond the power of the state, simply because the value of that railroad, as a whole, is created partly — and perhaps largely — by the interstate commerce which it is doing.[1] The United States Supreme Court declared the rule as to ascertaining the value of railroad property for taxation purposes to be as follows: When a railroad runs into or through two or more states, its value, for taxation purposes, in each is fairly estimated by taking that part of the value of the entire road which is measured by the proportion of the length of the particular part in that state to that of the whole road. Further, they held that the judgment of a state board of assessors, empowered to fix a valuation for taxation, could not be set aside by the testimony of witnesses that the valuation was other than that fixed by the board, where there was no evidence of fraud or of gross error in the system on which the valuations were made.[2]

[1] Cleveland, Cincinnati, Chicago & St. Louis Ry. Co. *v.* Backus, (1894) 154 U. S. 439. The court said: "It has been again and again said by this court that while no state could impose any tax or burden upon the privilege of doing the business of interstate commerce, yet it had the unquestioned right to place a property tax on the instrumentalities engaged in such commerce. See, among many other cases, Marye *v.* Baltimore & Ohio Railroad, 127 U. S. 117; Pullman's Palace Car Co. *v.* Pennsylvania, 141 U. S. 18."

[2] Pittsburgh, Cincinnati, Chicago & St. Louis Ry. Co. *v.* Backus, (1894) 154 U. S. 421. Mr. Justice BREWER, speaking for the majority of the court, said: "The stock and the indebtedness represent the property. As said by Mr. Justice MILLER in State Railroad Tax Cases, 92 U. S. 575, 605: 'When you have ascertained the current cash value of the whole funded debt, and current cash value of the entire number of shares, you have, by the action of those who above all others can best estimate it, ascertained the true value of the road, all its property, its capital stock and its franchises, for these are all represented by the value of its bonded debt and of the

A railroad company securing a state franchise to operate its road, afterwards obtaining a federal franchise, will not by the receipt of the latter be saved from the right of the state to tax the state franchise, the roadbed and other property of the company.[1] Taxes on the right of way of a railroad company cannot be avoided by the company by reason of errors in describing it in the assessment book.[2] The United States Supreme Court has held that the sum received by one railroad company from another for the use of its tracks was a toll within the meaning of a Pennsylvania statute, taxing gross receipts of railroad companies "for tolls and transportations."[3] Land belonging to a railroad

shares of its capital stock.' In Franklin County *v.* Nashville, Chattanooga, etc., Railway, 12 Lea, 521, 539, the Supreme Court of Tennessee, in a well-considered opinion, which was quoted with approval by this court in Columbus Southern Railway *v.* Wright, 151 U. S. 470, 479, thus referred to the means of ascertaining the value of a railroad track: 'The value of the roadway at any given time is not the original cost, nor, *a fortiori*, its ultimate cost after years of expenditure in repairs and improvements. On the other hand, its value cannot be determined by ascertaining the value of the land included in the roadway assessed at the market price of adjacent lands, and adding the value of the crossties, rails and spikes. The value of land depends largely upon the uses to which it can be put and the character of the improvements upon it. The assessable value for taxation of a railroad track can only be determined by looking at the elements on which the financial condition of the company depends, its traffic, as evidenced by the rolling stock and gross earnings in connection with its capital stock. No local estimate of the fraction in one county of a railroad track running through several counties can be based upon sufficient data to make it at all reliable, unless, indeed, the local assessors are furnished with the means of estimating the whole road. * * * This court has expressly held in two cases, where the road of a corporation ran through different states, that a tax upon the income or franchise of the road was properly apportioned by taking the whole income or value of the franchise, and the length of the road within each state, as the basis of taxation. The Delaware Railroad Tax Case, 18 Wall. 206; Erie Railway *v.* Pennsylvania, 21 Wall. 492.'"

[1] People *v.* Central Pacific R. R. Co., 105 Cal. 576; s. c., 38 Pac. Rep. 905.

[2] Cairo, V. & C. Ry. Co. *v.* Mathews, 152 Ill. 153; s. c., 38 N. E. Rep. 623. When the mode of computing a railroad company's tax will not vitiate the tax, see Cairo, V. & C. Ry. Co. *v.* Mathews, 152 Ill. 153; s. c., 38 N. E. Rep. 623.

[3] New York, Lake Erie & West. R. R. Co. *v.* Commonwealth of Pennsylvania, 158 U. S. 431; s. c., 15 Sup. Ct. Rep. 896. See State *v.* Stone, 119 Mo. 668; Herbert *v.* Railroad Company, 8 Del. 120. For rule as to power of the court in an action by a city to recover taxes of a railroad company upon a part of its road, brought within the city by an extension of its boundaries, in ascertaining the amount of taxes due, see Louisville & Nashville R. R. Co. *v.* Commonwealth, (Ky.) 30 S. W. Rep. 624. As to the effect of the

on which was situated its passenger and freight depots, round house, side tracks and terminal facilities has been held in Illinois to be properly assessable as "railroad track" under the statutes of that state, declaring that "such right of way, including the superstructures of main, side or second tracks and turnouts, and the stations and improvements of the railroad company on such right of way, shall be held to be real estate for the purpose of taxation and denominated 'railroad track' and shall be so listed and valued."[1] Trustees of bondholders in charge of a railroad whose main track was all outside the state of Illinois, but the trains of which were brought into the state over the tracks of another company, have been held to be "operating a railroad in this state" within the meaning of the statute of that state requiring those "owning, operating or constructing a railroad in this state" to return schedules of its taxable property.[2] The tax assessed upon a railroad company's property is a lien on all the property assessed, the property being assessed as a unit and the tax being due as a unit.[3]

Washington statute imposing a tax on "gross earnings" of railroad corporations in lieu of all other taxes, in exempting the property of the corporation from taxation, see Columbia & P. S. R. R. Co. *v.* Chilberg, 6 Wash. 612; s. c., 34 Pac. Rep. 163. As to what erections upon its land and improvements by a railroad corporation are so necessarily connected with its general business as to come within a statutory exemption of its property from general taxation, see Chicago, St. Paul, M. & O. Ry. Co. *v.* Bayfield County, (Wis.) 58 N. W. Rep. 245. As to railroads taxable under the Constitution of Florida of 1868, see Bloxham *v.* Florida Central & P. R. R. Co., (Fla.) 17 So. Rep. 902.

[1] Quincy, O. & K. C. Ry. Co. *v.* People, (Ill.) 41 N. E. Rep. 162.

[2] Ibid. That a railroad corporation operating a railroad from a point in the state to a point in another state, being liable to the tax prescribed on gross earnings under the New York statutes, as a tax on franchise, see People ex rel. Dunkirk, Alleghany Valley, etc., R. R. Co. *v.* Campbell, 74 Hun, 210; s. c., 26 N. Y. Supp. 832; 56 N. Y. St. Repr. 358; citing People ex rel. Pennsylvania R. R. Co. *v.* Wemple, 138 N. Y. 1; People *v.* Home Ins. Co., 92 N. Y. 328; People ex rel. Southern Cotton Oil Co. *v.* Wemple, 131 N. Y. 64. In Maricopa & Phœnix R. R. Co. *v.* Arizona Territory, 156 U. S. 347, where the United States government, through congress, had granted to the railroad corporation, organized under the laws of the territory, a right of way over an Indian reservation within the territory, the road being constructed entirely within the territory, it was held that the part of the road within the reservation was subject to taxation by the territorial government.

[3] Maricopa & P. R. R. Co. *v.* Territory of Arizona, 156 U. S. 347; s. c., 15 Sup. Ct. Rep. 391. As to exemption of a railroad company from taxation for five years under Kentucky statute, see Commonwealth *v.* Louis-

§ 586. **Taxation of insurance corporations.**— The Kansas Supreme Court has held the reserve fund of a mutual life assotion, organized on the co-operative plan, it having no capital stock, subject to taxation in that state.[1] They also held that the contingent liabilities of the association to the holders of its policies, were not such indebtedness of the corporation as could be deducted from the credits of the association subject to taxation.[2]

ville, St. Louis & K. Ry. Co., (Ky.) 31 S. W. Rep. 464. For illustrations of exemptions of railroad corporations from taxation which would not relieve them from assessments for local improvements, or special taxes for street pavements adjacent to their right of way, see Lake Shore & Michigan Southern Ry. Co. *v.* City of Grand Rapids, (Mich.) 60 N. W. Rep. 767; Illinois Central R. R. Co. *v.* City of Decatur, 154 Ill. 173; s. c., 38 N. E. Rep. 626. See, also, Commonwealth *v.* Railroad Company, 95 Ky. 60; Chicago, St. P., M. & O. Ry. Co. *v.* Bayfield County, 87 Wis. 188; State *v.* District Court, 54 Minn. 34; Fargo & S. W. R. R. Co. *v.* Brewer, 3 N. Dak. 34; Commonwealth *v.* Railway Company, 93 Ky. 430.

[1] Kansas Mutual Life Association *v.* Hill, Treasurer of Brown County, 51 Kans. 636.

[2] Ibid. The court's attention was called upon this point to Insurance Company *v.* Lott, 54 Ala. 499, and Equitable Life Ins. Co. *v.* Board of Equalization, 74 Iowa, 178; s. c., 37 N. W. Rep. 141, upon which the association's counsel relied, was distinguished by the court in these words: "The statute of Iowa allows a taxpayer to deduct his indebtedness from the amount of money or credits which he is required to list, and in that respect is quite unlike our own, which only allows such deduction to be made from credits not secured by liens on real estate, nor due from a bank on demand. The plaintiff in that case was a stock company to which its stockholders had contributed on their shares $100,000. The court regarded the shares as taxable at their cash value in the hands of the stockholders, and that this cash value would be augmented by whatever accumulations of profit the company held, to which they would be entitled in case of distribution. In the plaintiff company there are no stockholders. The policies issued by the plaintiff in that case were not forfeited by failure to pay premiums after two payments, but a paid-up policy was issued for an amount fixed by the terms of the policy. The court held the reserves on such policies debts owing by the company. In this case no such policies are outstanding. On the other hand, there are many authorities which hold that the contingent liabilities of insurance companies, both life and other, on policies outstanding before loss occurs, are not debts within the meaning of the statute, which may be deducted from the credits of the company. 1 Desty Tax. § 79; Insurance Co. *v.* Cappellar, 38 Ohio St. 560; Kenton Ins. Co. *v.* City of Covington, 86 Ky. 213; s. c., 5 S. W. Rep. 461; People *v.* Davenport, 91 N. Y. 574; People ex rel. *v.* Commissioners, 76 N. Y. 64; Fire Ins. Co. *v.* Parker, 35 N. J. Law, 575; Sun Mut. Ins. Co. *v.* Mayor, etc., of New York, 8 N. Y. 241. The general rule is that all property must bear its share of taxation, unless expressly exempted therefrom. * * * A contingent liability which is not susceptible of computa-

An insurance corporation, vested by its charter "with all the powers, privileges and immunities" of an older existing corporation, the Supreme Court of Tennessee held to be vested with a valid exemption from taxation contained in the charter of the older one.[1] But should the charter clothe the corporation "with all the rights and privileges" of such older existing corporation, without more, those words would not carry the exemption of the older corporation to the later one.[2] The Supreme Court of Tennessee has held that under a clause of the charter of an insurance company, that "there shall be a state tax of one-half of one per cent upon the amount of capital paid in," the capital stock, and not the shares, was taxed; and that under the charter provision the capital stock was exempted by implication from all taxation, whether state, county or municipal, other than the charter tax. This exemption, however, they held did not extend to the shares of stock.[3] Where corporate officers were in default in furnishing to the assessor of taxes the names of shareholders, the assessor assessed the shares of stock to "unknown owners." The Supreme Court of Tennessee held that the tax so assessed could be collected either by direct suit against the corporation, especially if it was a dividend-paying corporation, or by suit against the corporation and its officers, seeking discovery of the names of its shareholders, in order that they might be made parties by the supplemental bill.[4]

tion is not a debt owing in good faith which may be deducted from credits under the tax law. * * *"

[1] Memphis *v.* Phœnix, etc., Insurance Co., 91 Tenn. 566.

[2] Ibid. The court referred to Railroad Co. *v.* Hicks, 9 Bax. 442; State *v.* N. C. & St. L. Ry., 12 Lea, 583; Railroad Company *v.* Hamblen County, 102 U. S. 273; Wilson *v.* Gaines, 103 U. S. 417. As to exemptions of insurance corporations from taxation under statutes, see People, etc., *v.* Reliance Marine Insurance Co. (Lim.), 70 Hun, 554; Brennan *v.* Mississippi Home Insurance Co., 70 Miss. 531.

[3] Memphis *v.* Home Insurance Company, 91 Tenn. 558; citing Memphis *v.* Union & Planters' Bank, 91 Tenn. 546; Union Bank *v.* State, 9 Yer. 490; St. R. Co. *v.* Morrow, 87 Tenn. 406; Memphis *v.* Ensley, 6 Bax. 553; Gas Light Co. *v.* Nashville, 8 Lea, 406; Farrington *v.* Tennessee, 95 U. S. 679; Tennessee *v.* Whitworth, 117 U. S. 136.

[4] Memphis *v.* Home Insurance Co., 91 Tenn. 558.

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GENERAL INDEX.

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